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## Introduction

### Overview

Most Americans are unaware of the impact the commodity futures and option markets have on their everyday lives. Properly functioning futures and option markets serve vital price discovery and “hedging” functions that are essential to maintaining a healthy capital-based economy. This means that the prices established by these markets affect how much we pay for our food, our clothing, and our shelter.

Because of their pervasive nature, futures and option markets that function improperly can have a devastating effect on our lives. Therefore, the markets must be protected against manipulation, abusive trading practices, and fraud—the elements that cause improper market function. Doing so not only encourages the economic competitiveness, efficiency, and integrity of the markets, but also, more importantly, protects the American public from the detrimental forces seeking to gain monetarily at their expense.

### Background

Understanding the impact of the futures and option markets on the lives of all Americans, Congress in 1974 passed the Commodity Futures Trading Commission Act of 1974, which created the Commodity Futures Trading Commission (the Commission or CFTC) as an independent agency with the mandate to regulate commodity futures and option markets in the U.S. The Commission’s mandate was renewed and/or expanded in 1978, 1982, 1986, 1992, and 1995. In December 2000, the Commission was reauthorized by Congress and the President through fiscal year (FY) 2005 with the passage of the Commodity Futures Modernization Act of 2000 (CFMA).

### Impact of Commodity Futures Modernization Act

The CFMA transformed the Commission from a front-line regulatory agency to an oversight regulator. Although the Commission’s approach to regulation has consequently changed, its mission remains the same. The CFTC continues to be responsible for fostering the economic utility of futures markets by encouraging their competitiveness and efficiency, ensuring their integrity, and protecting market participants against manipulation, abusive trading practices, and fraud. Through effective oversight regulation, the CFTC enables the commodity futures markets better to serve their vital function in the Nation’s economy—providing a mechanism for price discovery and a means of offsetting price risks.

### Oversight of U.S. Futures Industry

Futures contracts for agricultural products have traded in the U.S. for over 150 years. In recent years, futures trading has expanded rapidly into many new markets, beyond the domain of traditional physical and agricultural commodities. Futures and option contracts are offered on a vast array of financial instruments, including foreign currencies, U.S. and foreign government securities, and U.S. and foreign stock indices.

Through its continued leadership role in the oversight of the U.S. futures industry, the Commission achieves its mandate by relying on several oversight actions:

- ❖ Enforcement—to police the futures and option markets for conduct that violates the Commodity Exchange Act (CEA) and Commission regulations.
- ❖ Market Surveillance—to survey the futures and option markets to ensure that they reflect the forces of supply and demand for the underlying commodity and are free of disruptive activity.
- ❖ Rulemaking, Auditing, and Reviewing—to protect the economic functions of the market, to protect market users, to foster open, competitive and financially sound markets, and to promote an effective, flexible regulatory environment, responsive to evolving market conditions.

Some of these interventions and actions reside entirely within the Commission, but the work of the Commission also involves significant partnering with local, state, national, and international authorities and with the futures industry. At the same time, some activities are internal, such as financial management, procurement, information resources management, personnel; without which the Commission could not operate or hope to achieve its goals.

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## Message from the Acting Chairman

Keeping pace with change has never been more significant than it is today at the CFTC. The unprecedented growth and complexity of the futures and options industry has not only been an exciting challenge, it has validated the past few years of hard work and dedication of the agency to provide the most flexible and responsive oversight structure possible. The results of our efforts are presented in this first CFTC Performance and Accountability Report.



This report is a result of meeting the requirements of the Accountability of Tax Dollars Act of 2002, in which agencies must prepare and submit to Congress, the Office of Management and Budget (OMB), and the public, annual audited financial statements and performance results. The passage of the Accountability of Tax Dollars Act has improved the financial performance through the integration of budget and performance results.

I am pleased to present the CFTC's first Performance and Accountability Report summarizing our achievements and challenges for FY 2004, and certify with reasonable assurance that, except for one material non-conformance regarding asset management specifically identified in the management control section of this report, our agency's systems of management control, taken as a whole, comply with the Federal Managers' Financial Integrity Act of 1982. I also certify that our agency is in substantial compliance with applicable Federal accounting standards and the U.S. General Ledger at the transaction level and with Federal financial system requirements. I am confident that the CFTC's financial and performance data is reliable, accurate, and consistent.

The agency's first independent audit conducted by KPMG LLP, under oversight of the Office of the Inspector General, has been conducted and reported on. The report highlights that we have received an unqualified (clean) opinion on our balance sheet. We are pleased with these initial results and will continue our efforts in FY 2005 to make the recommended improvements to our internal controls as discussed in the auditor's report.

As we improve our ability to measure progress towards our performance objectives, keeping pace with change will continue to be our challenge. The Commission stands ready to work with the Congress, other regulators, and market participants to ensure that our regulatory structure keeps up with the marketplace; and that our future Performance and Accountability Reports provides you with the results of our progress in meeting these challenges.

A handwritten signature in black ink, appearing to read 'Sharon Brown-Hruska'.

Sharon Brown-Hruska  
Acting Chairman  
November 17, 2004

## About This Report

The CFTC's *FY 2004 Performance and Accountability Report* is the first such report published by the Commission. This document is comprised of three primary sections:

### ❖ Management's Discussion and Analysis

The Management's Discussion and Analysis (MDA) is an overview of the entire Report, as supported and detailed in the Performance Section and Financial Section. The MDA presents performance, budget and financial highlights for FY 2004, as well as the Inspector General's discussion and analysis. In addition, the MDA addresses compliance with legal and regulatory requirements and existing or possible effects and challenges facing the Commission in the future.

### ❖ Performance Section

This Section compares the Commission's performance to the annual goals as set forth in the CFTC Strategic Plan. For more information on this section, please contact Emory Bevill, Deputy Director for Budget and Planning at 202-418-5187.

### ❖ Financial Section

This Section is comprised of the Commission's financial statements and related Independent Auditors' report. For more information on this section, please contact Jeanne Ring, Deputy Director for Accounting and Financial Systems at 202-418-5185.

An electronic version of this document is available on the Internet at [www.cftc.gov/cftc/cftcreports.htm](http://www.cftc.gov/cftc/cftcreports.htm). The Commission's strategic and performance plans are also available at this Web site.

Questions and comments about this document can be directed to Emory H. Bevill, Deputy Director, Budget and Planning at 202-418-5187, via e-mail at [ebbevill@cftc.gov](mailto:ebbevill@cftc.gov).



# Management's Discussion and Analysis

FY 2004 Performance and Accountability Report





## Mission and Organization

### CFTC Mission

In December 2000, the CFMA transformed the Commission from a front-line regulatory agency to an oversight regulator. Although the Commission's approach to regulation has consequently changed, its mission remains the same—to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of commodity futures and options, and to foster open, competitive, and financially sound commodity futures and option markets.

#### Mission Statement, Strategic Goals and Outcome Matrix

##### Mission Statement

*The mission of the CFTC is to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of commodity futures and options, and to foster open, competitive and financially sound commodity futures and option markets.*

##### Goal One

*Ensure the economic vitality of the commodity futures and option markets.*

##### Outcomes

1. Markets that accurately reflect the forces of supply and demand for the underlying commodity and are free of disruptive activity.
2. Markets that are effectively and efficiently monitored to ensure early warning of potential problems or issues that could adversely affect their economic vitality.

##### Goal Two

*Protect market users and the public.*

##### Outcomes

1. Violations of Federal commodities laws are detected and prevented.
2. Commodities professionals meet high standards.
3. Customer complaints against persons or firms falling within the jurisdiction of the Commodity Exchange Act are handled effectively and expeditiously.

##### Goal Three

*Ensure market integrity in order to foster open, competitive, and financially sound markets.*

##### Outcomes

1. Clearing organizations and firms holding customer funds have sound financial practices.
2. Commodity futures and option markets are effectively self-regulated.
3. Markets are free of trade practice abuses.
4. Regulatory environment is responsive to evolving market conditions.

## Mission Highlights

Through effective oversight, the CFTC enables the futures markets to serve the important function of providing a means for price discovery and offsetting price risk.

### **An Important Mission in the Ever-Changing World of Finance**

- ❖ The mission of the CFTC is to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of commodity and financial futures and options, and to foster open, competitive, and financially sound futures and options markets.

### **Futures and Option Contracts**

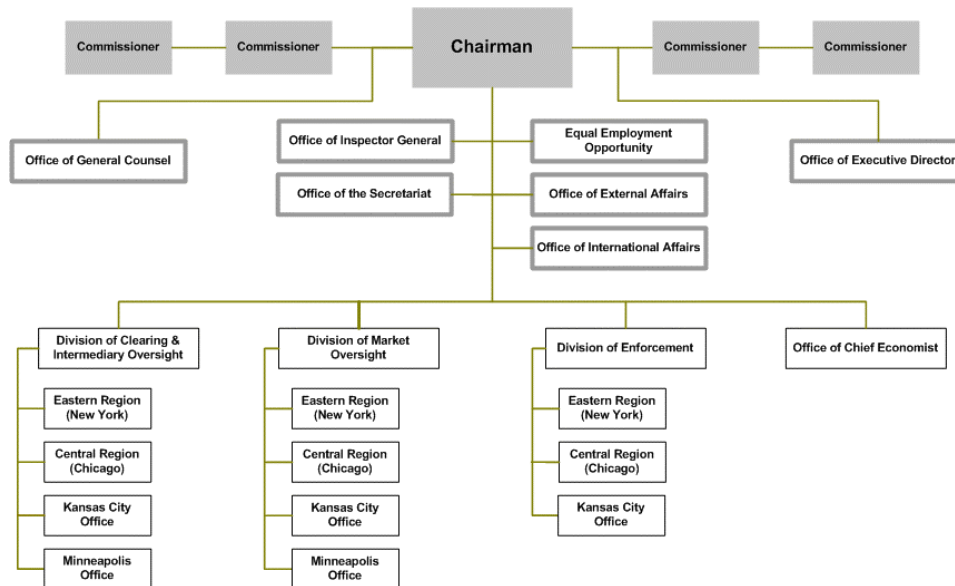
- ❖ Futures contracts for agricultural commodities have been traded in the U.S. for more than 150 years and have been under Federal regulation since the 1920s. In recent years, trading in futures contracts has expanded rapidly beyond traditional physical and agricultural commodities into a vast array of financial instruments, including foreign currencies, U.S. and foreign government securities, and U.S. and foreign stock indices.

### **Evolving Mission and Responsibilities**

- ❖ Congress created the CFTC in 1974 as an independent agency with the mandate to regulate commodity futures and option markets in the United States. The agency's mandate has been renewed and expanded several times since then, most recently by the CFMA.
- ❖ Today, the CFTC assures the economic utility of futures markets by encouraging their competitiveness and efficiency, ensuring their integrity, protecting market participants against manipulation, abusive trading practices, and fraud, and ensuring the financial integrity of the clearing process. Through effective oversight, the CFTC enables the futures markets to service the important function of price discovery and offsetting price risk.

## Organization

### Commodity Futures Trading Commission Organization Structure



### CFTC Organization

- ❖ The Commission consists of five Commissioners appointed by the President to service staggered five-year terms. The President, with the consent of the Senate, designates one of the Commissioners to serve as Chairman. No more than three Commissioners at any one time may be from the same political party.

### A Highly Professional and Diverse Staff

- ❖ The Commission employs top-notch professionals with strong academic records and excellent analytical and problem-solving skills for this important work:
  - Attorneys at the Commission work on complex and novel legal issues in litigation, regulation, and policy development. Attorneys participate in administrative and civil proceedings, assist U.S. Attorneys in criminal proceedings involving futures law violations, and provide legal advice to the Commission on policy and adjudicatory matters.
  - Auditors examine records and operations of futures exchanges and firms for compliance with CFTC rules on financial requirements and trade practices.
  - Economists evaluate filings for new futures and option contracts and amendments to existing contracts to ensure they meet the Commission's regulatory standards. Economists also analyze and advise the Commission on the economic effect of various Commission and industry actions and events.

- Futures Trading Specialists/Investigators perform regulatory and compliance oversight and conduct investigations of alleged fraud, market manipulations, and trade practice violations. They may also appear as expert witnesses in administrative or civil proceedings, or assist state or other Federal law enforcement agencies in dealing with futures-related violations.
- Management professionals support the CFTC mission by performing strategic planning, information technology, human resources, staffing, training, accounting, budgeting, contracting, procurement, and other management operations.

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## Performance Summary and Highlights

During FY 2004, the CFTC has made substantial progress in advancing our vision of preserving and protecting the vital economic role played by America's futures industry and we have continued to demonstrate our commitment to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of commodity futures and options, and to foster open competitive, and financially sound futures and option markets.

Among our most noteworthy accomplishments during FY 2004 are:

- ❖ Progress in implementing the CFMA including:
  - Submitting a report to the Federal Reserve Board concerning the exercise of authority delegated by the Board to the Commission and the Security and Exchange Commission (SEC) to prescribe customer margin rules for security futures products (SFP).
  - Signing of a Memorandum of Understanding (MOU) between the SEC and the Commission to clarify the ability of each agency to conduct inspections of notice-registered intermediaries, exchanges, and limited purpose national securities associations.
- ❖ Investigating alleged misconduct in the Energy Markets. The investigation has focused on energy trading firms that have allegedly engaged in the reporting of false, misleading or knowingly inaccurate market information, including price or volume information, attempted manipulation or manipulation, and/or "round-tripping," a risk-free trading practice that produces wash results and the reporting of non bona fide prices in violation of the Act.
- ❖ Fighting Foreign Currency (forex) Trading Fraud. Under the CFMA it is unlawful to offer off-exchange forex futures or option contracts to retail customers unless the counterparty is a CFMA-enumerated regulated financial entity such as a futures commission merchant (FCM) or a financial institution. The Commission has brought enforcement actions against both registered firms and unregistered "bucket shops."
- ❖ Protecting investors from unscrupulous commodity trading advisors (CTAs) and commodity pool operators (CPOs) that promise great riches with little risk and then often stealing investor funds.
- ❖ Investigating Natural Gas Price Spikes. The Commission concluded a seven-month investigation of the sharp upward movement in prices in the natural gas market that occurred in late 2003. The investigation did not uncover evidence that any entity or individual engaged in activity with an intent to cause an artificial price in natural gas in late 2003.
- ❖ Investigating the Cattle Markets in Connection with the Bovine Spongiform Encephalopathy (BSE) or "mad cow" scare. The Commission

opened an investigation in last December that is looking into the possibility that certain commodity traders had advance announcement that “mad cow” disease had been found in a cattle herd in the northwestern U.S. The investigation seeks to determine whether news of the announcement was leaked in advance from government sources.

- ❖ Continued U.S. leadership in setting international standards for effective regulation through active participation in the International Organization of Securities Commission (IOSCO) efforts to develop best practices principles in areas that are intended to help foster higher international regulatory standards and increase access to markets and products.
- ❖ Assessing and responding to the impact of technological change on methods of transacting business on futures exchanges and a proliferation of designation applications for new electronic futures exchanges.
- ❖ Reviewing 200 new futures and option contracts based on a wide variety of underlying physical products, financial instruments, and economic indexes – many of which represent innovative approaches designed to meet specialized hedging needs of producers and firms in various industries. In addition, 25 SFPs were filed during FY 2004.
- ❖ Refining Intermediary Policy, for example: Part 30 Rule Clarification; revising risk-based capital requirements; reviewing the issue of remote clearing and how it may relate to cross-border clearing arrangements.
- ❖ Developing New Oversight Examination Programs -- in close consultation with other federal financial regulators and certain overseas financial supervisors – to enhance supervision of exchanges, clearinghouse and other self-regulatory organizations (SROs) with risk-based examination cycles and risk-focused reviews.
- ❖ Modernizing and Streamlining Financial Filing Requirements that modernize certain financial reporting for Introducing Brokers (IBs) and FCMs.
- ❖ Revising the Form 1-FR-FCM and Instruction Manual to reflect the new risk-based capital rules, as well as numerous rulemaking and interpretations that have been issued by the Commission. This revision is the first time the manual has been revised since the Commission issued it in 1989.

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## Future Effects and Challenges

### Clearing and Intermediary Oversight

Increased numbers of registrants, particularly derivatives clearing organizations (DCOs) and firms engaged in retail forex transactions, will challenge the resources of the Clearing and Intermediary Oversight program.

### Regulation of Intermediaries

The Clearing and Intermediary Oversight program will continue to enhance an effective oversight framework for intermediaries. Staff will continue its efforts to streamline and modernize pool operator and trading advisor regulation, and to reduce or eliminate regulatory burdens where they are not needed, such as where the level of futures trading is minimal and where pool participants or advisory clients are highly sophisticated. The Commission adopted in July 2004, a proposal developed by staff to clarify availability of the registration relief provided by recently adopted Rule 4.13(a)(3). In addition, staff is preparing rulemaking proposals that would define the term “client” of a CTA, and would specify situations in which the registration exemption for CTAs providing standardized trading advice would not be available for a CTA that manages client accounts pursuant to a letter of direction or other written authorization in favor of either the CTA or an FCM, IB, or associated person (AP). The latter proposal would further specify situations in which a CTA managing client accounts pursuant to a letter of direction or other written authorization would be an account controller for the purposes of receiving account statements and other documentation.

### Coordination with Other Regulators

The Clearing and Intermediary Oversight program will continue to coordinate with the SEC regarding regulation of SFP trading and rationalizing the requirements applicable to persons, such as investment advisers, doing business under both CFTC and SEC regulatory frameworks. The program will also continue to work with the National Futures Association (NFA) and the National Association of Securities Dealers in developing an appropriate proficiency examination for persons engaging in security futures trading. Joint regulation with the SEC of SFPs has involved unforeseen challenges, and the Commission will consider ways to alleviate undue burdens on the industry so that the market for this new product may continue to develop. Staff has initiated and will continue discussions with regulatory authorities in the United Kingdom (U.K.) and Germany concerning coordinating regulatory oversight of cross-border business, in particular, the activities of the LCH-Clearnet and Eurex Clearing AG.

### Retail Forex Trading

The CFMA clarified the Commission’s jurisdiction over off-exchange retail forex trading. Going forward, the Clearing and Intermediary Oversight program will continue to work with NFA in developing guidance for persons who engage in retail off-exchange forex futures and options trading, in designing and conducting audits, and in verifying compliance with required adjusted net capital requirements for firms engaged in retail forex transactions. This will continue to be a particular challenge given the limited jurisdiction provided to the Commission under the CFMA, and the recent decision in the *Zelener* case, and the Commission will consider whether statutory changes should be sought.

### Implementation of the USA PATRIOT Act

Commission staff will continue working with Treasury in finalizing proposed anti-money laundering (AML) program rules for CTAs, investment advisors (IAs) and unregistered investment companies. The final rules are currently being drafted. Staff also has been working with the SEC and other federal financial agencies in drafting interpretations of the customer identification rules and a proposed no-action position concerning the customers of certain CTAs and IAs. The first tier of the interpretations for the futures industry was issued on June 14, 2004. Staff will also continue to work with Treasury in a process for sharing information about possible terrorists and money launderers. As part of this process, Commission staff maintains and updates a list of FCMs and contact persons, which Treasury then uses when issuing a list of possible money launderers and terrorists on a biweekly basis. The Commission recognizes that, although this process has not been part of its mission historically and presents certain unique aspects, the Commission must rise to the challenge posed by money launderers and terrorists, and prevent them from using futures markets for illegal purposes.

### General Counsel

Continuation of the record growth and globalization of the futures industry in recent years will impact the Office of General Counsel (OGC) in many ways. With increasing industry growth has come a proliferation of new and innovative trading platforms and products. This trend will call for increasing OGC analysis of novel and complex legal questions, particularly with respect to cross-border trading. The recent trend of increasing case filings by the Division of Enforcement places demands on all program areas within OGC – from legal review of proposed charges and settlements, to appellate litigation work, to adjudicatory matters with respect to administrative cases. OGC also must continue to meet the challenge of maintaining its readiness to respond to unpredictable events initiated by third parties, such as service of judicial subpoenas, commencement of bankruptcy proceedings, challenges to Commission personnel actions, and Freedom of Information Act (FOIA) filings, to name just a few. OGC anticipates increasing activity with the upcoming legislative reauthorization process, though the pace and intensity of that process are uncertain. OGC also anticipates a continuation of the heightened level of activity that has resulted from the added responsibilities imposed on the Office with the enactment of the CFMA (including cooperative regulatory and enforcement efforts on both an inter-agency and international basis), and responsibilities assumed by the Office as part of internal reallocations of certain program functions within the agency (e.g., compliance with ethics requirements, Paperwork Reduction Act obligations, etc.).

### Market Oversight

The promotion of responsible innovation and fair competition was added to the purpose of the Act under Section 3(b) by the CFMA, and the Market Oversight program will continue to work with a variety of markets that are interested in innovation or in opening up current markets to greater competition. These markets may be currently regulated by the Commission or are interested in becoming regulated. The Market Oversight program will also continue to work with foreign regulators, in order to develop appropriate responses to innovation and competition. This is a particular challenge since many of the proposals brought to the attention of the Market Oversight program raise novel and complex issues.

In addition, since the passage of the CFMA, there has been a large increase in the number of novel trading mechanisms and innovative products, including instruments based upon economic occurrences, the outcome of political events, and the



conduct of individuals. The Market Oversight program will have to devote an increasing amount of resources to giving direction to the industry with regard to Commission jurisdiction over these matters, whether through rulemakings, interpretive letters, or no-action letters. Given the sophisticated nature of the financial engineering that accompanies these innovations, such jurisdictional determinations will require extensive case-by-case analyses by staff economists and attorneys.

Large trader reporting and exchange data reporting in fulfillment of market surveillance requirements will continue to grow in complexity as new exchanges and new types of products come into existence. FY 2004 saw the introduction of innovative products such as fixed payout binary options, daily expiring futures contracts, and negatively priced contracts as well as the start up of several new exchanges. Staff will work with reporting firms and exchange personnel to attempt to implement solutions for novel products that will conform to existing industry data reporting practices. Division of Market Oversight (DMO) staff will coordinate work in systems design, testing, and data communications between CFTC and industry information technology groups. When necessary, DMO and OIRM will enhance the ISS (Integrated Surveillance System) to provide the tools necessary for surveillance of any new exchanges or products. In addition to the possibility of new exchanges, data reporting by exempt commercial markets is expected to begin in FY 2005. This will require implementation of a new data record format for reporting by these markets, ISS database extensions, and new ISS reporting tools for the analysis of products of these markets.

In order to meet the changing demands of the marketplace, driven by growth in electronic trading, novel products and intermarket trading strategies, the Commission is developing a new automated trade practice surveillance system to more efficiently and effectively detect illegal trading activity. The new surveillance system will identify possible trading abuses for referral to exchanges and the Division of Enforcement, and will support Commission investigations and litigation involving manipulation and trade practice abuses. A new, robust system also will allow identification of inter-exchange violations which individual exchanges lack the capacity to detect, allow quicker access to and more sophisticated and customizable analysis of the full range of data supplied by exchanges with respect to electronic as well as open outcry trading, and enable meaningful Commission evaluation of the exchanges' own electronic surveillance systems. In designing and implementing the new system, Commission staff will combine custom-built components with available off-the-shelf software to give the Commission unqualified, immediate, and confidential access to all exchange-supplied data. It is estimated that the new system will take approximately two and one-half years to implement fully.

### Proceedings

The Office of Proceedings expects the number reparations filings to remain the same in FY 2006; however, if Proceedings receives a significant increase in the number of reparations cases filed, it could seriously challenge the staffing and fiscal resources of the Office. Some of the challenges that the Office of Proceedings may encounter if a significant increase in reparations complaints is experienced are:

- ❖ The overall processing time of reparations complaints in the Complaints Section may increase.

- ❖ The Proceedings Clerk's Office would also receive an increase in cases forwarded for the institution of a formal adjudicatory proceeding, significantly increasing the number of pleadings filed by parties, as well as an increase in the orders, rulings, and decisions issued by the ALJs and the Commission.
- ❖ The presiding officers' workload would also increase significantly. It is possible that the percentage of cases disposed of within one-year may decrease.
- ❖ The future effects of a possible increase in cases filed may challenge our budgeted resources (travel and transcripts costs would increase).
- ❖ The number of cases could possibly increase if the Commission assumes jurisdiction over new and unique types of instrument(s).
- ❖ The response time to requests for information and copies of documents may increase.
- ❖ The response time to FOIA and Privacy Act requests may increase.

#### Administrative Enforcement Cases

The Administrative Law Judges (ALJ) will continue to hear and decide administrative enforcement cases; however, a significant increase in the administrative enforcement cases would challenge the resources (staff and fiscal) of the Office of Proceedings. Some of the challenges that the Office of Proceedings would encounter if a significant increase in the number of administrative enforcement cases filed were experienced are:

- ❖ The Proceedings Clerk's Office would experience an increase in the number of pleadings filed by parties to the cases, as well as an increase in the orders, rulings, and decisions issued by the ALJs and the Commission.
- ❖ The ALJs' overall workload would also increase significantly. The future effects of a possible increase in cases filed may challenge our budget resources (travel and transcripts costs would increase).
- ❖ The number of cases could possibly increase if the Commission obtains jurisdiction over new and unique types of instrument(s).

#### Optimal Staffing

Potential obstacles to the goal of optimal staffing include: numbers of retirements that are either much larger or much smaller than anticipated; job market that is either much more or much less competitive than at present; rapid change in industry, beyond our ability to hire or develop staff competencies needed to respond; and insufficient funding to support needed full-time equivalent (FTE), workforce planning and succession strategies, etc.

#### Achieve Full Funding for Pay Parity

Potential obstacles to the goal of pay parity include: increases by our benchmark financial regulatory agencies, based on fees from regulated industries, that we cannot afford to match; difficulty in allocating staff and other administrative overhead needed to support contracting for complex benefit packages found at larger FIRREA agencies; and lack of consensus on which of the various FIRREA models to follow.

### International Affairs

The Commission's International Affairs program anticipates that the trend of futures exchanges, clearing organizations and intermediaries expanding their global relationships through linkages and other commercial ventures, as well as through seeking direct recognition abroad, will continue to accelerate. Because these global relationships often take place in multiple jurisdictions, their proper regulation necessitates enhanced cooperation with multiple foreign regulators who may be best placed to assure the financial and market integrity of various aspects of the relevant transactions. The Commission anticipates that this trend will continue and may place greater demands on the Commission to enhance its regulatory and enforcement cooperative efforts both not only on individual bilateral and multilateral bases, but also on broader multilateral international forums such as IOSCO, Council of Securities Regulators of the Americas (COSRA) and the Council of European Securities Regulators to negotiate international principles and regional supervisory approaches. The Commission to date has found it difficult to host meetings of IOSCO and other international organizations in which it participates.

There continues to be greater focus among international regulators and international financial institutions such as the International Monetary Fund and World Bank to continue to develop international regulatory standards and to enhance assessment efforts to ensure that the international standards developed by standard setters such as IOSCO are in fact implemented. The Commission has participated in such standard setting exercises, such as chairing the IOSCO Implementation Committee, and finds such participation of great value to assure that standards remain high and consistent with its approach. The Commission anticipates that it may need greater resources to adequately cover and staff these activities should they accelerate.

Finally, the Commission continues to receive requests to provide technical assistance, particularly as a result of the increasing focus noted above on the assessment of jurisdictions' efforts to implement international standards. Such requests will place increasing demands on the Commission's limited resources.

### Information Resources Management

The Commission plans to design and implement a robust Commission-wide Asset Management Program to manage Commission assets throughout the asset's life-cycle, from requisition to surplus. This complex and challenging effort is critical to the Commission's daily operational efficiency and effectiveness. This effort will allow the Commission to save valuable resources, time and money, while building better business operations and enhancing accountability. Organizational change and the implementation of new processes are key challenges the Commission will face executing this effort. These changes include: 1) assigning matrix functional responsibility, 2) defining accountability 3) developing policies and procedures, and 4) implementing tracking processes and tools. Once the business processes are streamlined and redesigned, a technology solution will be applied. Although the program is still in its infancy and office responsibilities are still being defined, the positive effect of the success of this program will be felt across the Commission for many years to come.

### Conversion to Commercial Mail Process

The Office of Management Operations will be converting the current mail handling and payment process through the Official Mail Accounting System to a

commercial payment process in accordance with the General Services Administration regulation. The conversion must be coordinated with the U.S. Postal Service, Commission financial and mail managers, and the commercial postal vendor. It will require a review of all mail meters and equipment upgrades to support this initiative. As part of the review process, it will be determined how best to meet the postal needs of each location. The Commission will also need to arrange permits with the U.S. Postal Service in each location. The ultimate benefits of this conversion will be to: track postage cost in real time; measure performance; identify opportunities to save money; identify instances of potential fraud; increase the ability to react quickly to problems; and to streamline operations and improve productivity.

#### Kansas City Regional Office Relocation

With Kansas City's current growth, and its projected FY 2005 growth, the office relocated to larger office space in October 2004. In addition to the change in space requirements, the responsibilities and activities have increased with the addition of the Enforcement division. The Office of Management Operations was challenged with relocating the office, establishing the required support services, as well as providing ongoing operational support.

#### Asset Management

The Commission, with contractor assistance, is designing a Commission Asset Management Program to manage Commission assets throughout their lifecycle from requisition to surplus while taking into consideration all perspectives in order for the Commission to save time, money, and allow for smoother, more successful operations. Although the program is still in its infancy and office responsibilities are not clearly defined, the Office of Management Operations will be responsible for physical assets other than IT related items.

In order for a successful program, there must be organizational changes, such as:

- ❖ Assigning matrix functional responsibility
- ❖ Identifying accountable parties
- ❖ Developing formal agency policies
- ❖ Implementing tracking processes and tools.

Once the processes are streamlined and redesigned to meet requirements, automation will be applied.

#### Business Continuity Plan

Under the umbrella of the Continuity of Operations Plan, the Office of Management Operations is currently developing a Business Continuity Plan. This contingency plan, which will be used in the event that the Commission is not able to work at our current locations, will support the recovery and continuity of the Office of Management Operations' critical business functions and the eventual restoration of normal operations.

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## Inspector General's Discussion and Analysis



Office of the  
Inspector General

### U.S. COMMODITY FUTURES TRADING COMMISSION

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**TO:** Sharon Brown-Hruska  
Acting Chairman

**FROM:** A. Roy Lavik *ARL*  
Inspector General

**DATE:** November 15, 2004

**SUBJECT:** Inspector General's Assessment Of The Most Serious Management Challenges Facing CFTC.

This letter is submitted in response to an October 18, 2002 memorandum from Mark Everson, Deputy Director for Management of the Office of Management and Budget. Part III of that memorandum entitled, "Financial Section (c) An Inspector General (IG) Summary of Serious Management Challenges" requires the Inspector General to provide a summary of the management challenges facing the agency that the IG considers to be serious and a brief assessment of the agency's progress in addressing those challenges.

#### Background

On January 24, 2000, Congress enacted the *Reports Consolidation Act of 2000* to provide financial and performance information in a more meaningful and useful format for Congress, the President, and the public. Included in the Act is the requirement that the Inspector General of each Federal agency summarize what he or she considers to be the most serious management and performance challenges facing the agency and assess the agency's progress in addressing those challenges. In accordance, with the *Reports Consolidation Act of 2000*, I am submitting, for the first time, my annual assessment of the major management challenges confronting the Commodity Futures Trading Commission (CFTC).

Congress left the determination and threshold of what constitutes a most serious challenge to the discretion of the Inspector General. As a result, I applied the following definition in preparing my statement:

Serious management challenges are mission critical area or programs that have the potential for a perennial weakness or vulnerability that, without substantial management attention, would seriously impact agency operations or strategic goals.



In Fiscal Year 2002, Congress passed the Accountability of Tax Dollars Act. This Act requires CFTC, along with numerous other federal entities, to have its financial statements audited annually. Fiscal Year 2004 is the first fiscal year that the CFTC's financial statements were audited. On January 15, 2004 the Office of Inspector General (OIG) hired an independent public accounting firm, KPMG, to conduct an audit of the CFTC's financial statements. This letter relied on the data contained in the audited financial statements as well as the agency's Performance and Accountability Report (PAR).

### **Serious Management Challenges**

The OIG reviewed all the management challenges listed by program areas as well as external challenges mentioned in the PAR. As a result of our review, the OIG concludes that management fairly stated the challenges faced by the agency and identified in the PAR. Nonetheless, the OIG identifies two management challenges that we consider to be the most serious management challenges facing the agency. Although the PAR identified challenges by program areas, the OIG adopted a broader, agency-wide, perspective in selecting two summary management challenges.

We have combined the agency's *Challenges in the Marketplace* and *Technological Challenges* into one challenge that we describe as *Technological Responses To Industry Dynamics*. In addition, Human Resource Planning to achieve *Optimal Staffing* (stated in the PAR) is the second of the two management challenges that the OIG considers to be the most serious management challenges facing the CFTC. These two management challenges in no way diminish other challenges identified by the agency but they ought to guide the agency's efforts in the near future.

### **I. Technological Responses To Industry Dynamics**

In the last decade, 815 new futures and option contracts were approved or certified by the CFTC. During that same time period exchange traded futures and options volume has dramatically increased to over one billion futures and options contracts traded annually on exchanges monitored by the CFTC. During the same period and continuing into the foreseeable future, it is doubtful that the agency's budget will experience an equal increase. Consequently, the OIG's concern is that management ought to devote the necessary resources to dramatically improve its use of technology to assist existing and future employees with their oversight responsibilities mandated by the Commodity Futures Modernization Act of 2000 (CFMA)

The CFMA under section 3(b) charged the agency with the promotion of responsible innovation and fair competition. Our review of the PAR leads us to conclude that the novel and complex issues raised by this mandate will challenge the agency to efficiently use its skilled economists and attorneys to evaluate innovative products likely to be introduced to the marketplace -- possibly via an electronic trading platform. Furthermore, the OIG recognizes that the agency has responded to this challenge by initiating the development of a new integrated surveillance system with the goal of increasing the productivity of staff in the Division of Market Oversight and Division of Enforcement. Such quick response is to be applauded; however, all new systems are fraught with the danger of delays and incorrect specifications, especially a new electronic market

surveillance system for a rapidly growing industry such as the futures and options industry. The OIG will actively monitor management's efforts to deliver an effective technological solution to meet its mandates under the CFMA.

Critical and appropriate observation by the OIG can spur the agency to embrace and successfully meet the technological challenges it faces from continued success of exchange traded futures and options products. In fact, the OIG has worked, proactively, with the Division of Enforcement in its efforts to adopt the electronic enforcement modernization project—E-Law, which will significantly increase the productivity of CFTC attorneys. The agency will soon adopt a new Asset Management Program to manage agency's assets throughout their lifecycle from requisition to surplus, which should aid the agency to save time, money, and safeguard its assets. This proposed electronic Asset Management system is a direct remedy for a finding (Lack Of Internal Controls For Fixed Assets) in the financial statement audit issued concurrently with this letter.

## **II. Human Resource Planning**

By March 2006, current estimates are that over twenty percent of CFTC staff will be eligible for retirement. This is a significant problem which requires a great deal of planning. The OIG is heartened by the agency's decision to establish a Human Capital Team and engage a consulting firm to assist it to catalogue current skills of existing employees and propose possible pathways for meeting this potential deficit that is likely to occur in Fiscal Year 2006.

In accordance with GAO's challenge to the executive branch to extend its evaluative horizon, the OIG is challenging this agency to focus not just on the present fiscal year human resource needs but broaden its evaluative envelope to include future trends and challenges. Proper succession planning and management efforts can help an organization become what it needs to be, rather than simply to recreate the existing organization. The agency must focus on strengthening both current and future organizational capacity to meet future externally imposed challenges. It must address specific human capital challenges, such as diversity, leadership capacity, and retention. Also, as stated in the PAR, the agency is challenged to effectively coordinate its staff with other government agencies, such as, the Department of the Treasury and the Securities and Exchange Commission.

In summary, the OIG's review of the PAR and familiarity with the organization lead us to conclude that the agency has clearly recognized the management challenges it is likely to face in Fiscal Year 2005. We believe that plans presently in place can properly address the challenges stated in the PAR. We look forward to evaluating the success of the agency in satisfying its regulatory mandates.



## Management Controls, Systems and Compliance with Laws

CFTC Statement of Assurance for FY 2004



### U.S. Commodity Futures Trading Commission

#### Fiscal Year 2004 Annual Assurance Statement

The Commodity Futures Trading Commission (CFTC) has completed its FY 2004 Federal Managers' Financial Integrity Act (FMFIA) annual report. This report reflects continuing progress in strengthening management and accountability controls, and improving financial management systems in support of CFTC's mission and the President's Management Agenda.

In the past year, our efforts to restructure the CFTC to better facilitate ongoing implementation of the Commodity Futures Modernization Act, as well as effect changes to become compliant with the President's Management Agenda, the Federal Information Security Reform Act, and the Accountability of Tax Dollars Act, have resulted in the identification of a material nonconformance in the agency's information asset management program.

As a result, I am able to certify with qualified assurance that, except for the material nonconformance specifically identified in this report, the CFTC is in compliance with the provisions of Sections 2 and 4 of the FMFIA. I have no evidence at this time to believe that actual management integrity of the Commission is materially weakened by these deficiencies.

The Commission continues to pursue vigorously the prompt resolution of all material weaknesses and non-conformances, and to reduce susceptibility to waste, fraud and mismanagement.

Sharon Brown-Hruska  
Acting Chairman



#### Federal Managers' Financial Integrity Act

The Federal Managers' Financial Integrity Act (FMFIA) requires agencies to institute management accountability and internal controls for program, operational, administrative, accounting and financial management functions. These controls must provide reasonable assurance that agency:

- ❖ Obligations and costs are in compliance with applicable laws;
- ❖ Funds, property and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and
- ❖ Revenues and expenditures are properly recorded and accounted for.

In addition, FMFIA requires the agency head to annually report on the adequacy of its management controls and conformance of its financial systems to federal regulations and standards. The report on its controls and financial systems is based on evaluations of its program, operational, administrative, accounting and financial management functions.

The CFTC's management control program is designed to comply with the requirements of FMFIA, including OMB Circular A-123, "Management Accountability and Control," OMB Circular A-127, "Financial Systems," and OMB Circular A-130, Management of Federal Information Resources. The management control program ensures:

- ❖ Programs achieve their intended results;
- ❖ Resources are used effectively and are consistent with the agency's mission;
- ❖ Programs and resources are properly safeguarded against waste, fraud and mismanagement;
- ❖ Information supports timely, complete and reliable decision-making; and
- ❖ Laws and regulations are followed.

Ongoing control reviews are conducted by the major divisions and offices of the Commission to ensure that systems and controls comply with the standards established by FMFIA. The results of these reviews are reported annually to the Acting Chairman and include:

- ❖ Management knowledge gained from daily operations;
- ❖ Audits of internal controls and financial statements;
- ❖ Financial management systems reviews;
- ❖ Office of the Inspector General and Government Accountability Office reports; and
- ❖ Other reviews, evaluations and related reports.

For FY 2004, the Acting Chairman issued a qualified statement of assurance that, other than a material non-conformance related to the agency's asset management system, the CFTC is in compliance with FMFIA. The Acting Chairman based this statement of assurance on management control reviews conducted by the major

## FY 2004 PERFORMANCE AND ACCOUNTABILITY REPORT

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divisions and offices of the Commission, financial systems reviews by the various offices of the Executive Director, a summary management review by the Executive Director, and a limited review process conducted by the Office of the Inspector General.

The material non-conformance related to the asset management system was originally reported in the CFTC's FY 2002 FMFIA report and updated in the agency's FY 2003 report. The FY 2004 assessment of this system determined that the material non-conformance continues to exist. The agency's remediation plan for bringing this system anticipates full compliance by FY 2007.

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## Budget and Financial Highlights

The Commission's balance sheet, which appears in the Financial Section of this Report, received an unqualified audit opinion issued by the accounting firm of KPMG LLP. This is the first year that the Commission financial statements have been audited by an independent accounting firm. Preparing these statements is a part of the Commission's goal to improve financial management and to provide accurate and reliable information that is useful for assessing performance and allocating resources. Commission management is responsible for the integrity and objectivity of the financial information presented in the financial statements.

The financial statements and financial data presented in this report have been prepared from accounting records of the CFTC in conformity with the U.S. generally accepted accounting principles (GAAP). U.S. GAAP for Federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB).

### Overview of Financial Position

**Assets.** The Commission had total assets of \$62.2 million at the end of FY 2004. The Commission's assets are summarized in the following table:

#### **Assets**

##### Intragovernmental:

Fund Balance with Treasury	\$ 26,304,227
Accounts Receivable	22,806
<b>Total Intragovernmental</b>	<b>26,327,033</b>

Custodial Fines and Interest Receivable, Net	35,402,939
Accounts Receivable	9,457
Equipment and Furniture, Net	340,210
Software, Net	149,428
<b>Total Assets</b>	<b>\$ 62,229,067</b>

**Liabilities.** The Commission had total liabilities of \$44.4 million at the end of FY 2004.

#### **Liabilities**

##### Intragovernmental:

FECA Liabilities	\$ 194,102
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##### With the Public:

Trade Accounts Payable	1,025,643
Accrued Funded Payroll and Benefits	2,282,462
Annual Leave	4,797,304
Actuarial FECA Liabilities	514,932
Custodial Liabilities	35,402,939
Contingent Liabilities	182,426
<b>Total Liabilities</b>	<b>\$ 44,399,808</b>

## FY 2004 PERFORMANCE AND ACCOUNTABILITY REPORT

**Ending Net Position.** The Commission had a net position of \$17.8 million at the end of FY 2004. The Commission's Net Position is summarized in the following table:

<b>Net Position</b>	
Cumulative Results of Operations	(5,199,126)
Unexpended Appropriations	23,028,385
<b>Total Net Position</b>	<b>17,829,259</b>

**Results of Operations.** The results of operations are reported in the Statement of Net Cost and the Statement of Changes in Net Position.

The Statement of Net Cost presents the Commission's gross and net cost for its strategic goals. The net cost of operations is the gross (i.e., total) cost incurred by the commission, less any earned revenue.

*Goal One: Ensure the economic vitality of the commodity futures and option markets*

	<b>Unaudited</b>
Intragovernmental Gross Costs	\$ 4,297,937
Less: Earned Revenue	(10,605)
<b>Intragovernmental Net Cost of Operations</b>	<b>4,287,332</b>
Gross Costs With the Public	27,124,106
Less: Earned Revenue	(9,032)
<b>Net Cost of Operations With the Public</b>	<b>27,115,074</b>
<b>Net Cost of Operations - Goal One</b>	<b>\$ 31,402,406</b>

*Goal Two: Protect market users and the public*

Intragovernmental Gross Costs	\$ 5,245,515
Less: Earned Revenue	(12,943)
<b>Intragovernmental Net Cost of Operations</b>	<b>5,232,572</b>
Gross Costs With the Public	33,104,237
Less: Earned Revenue	(11,023)
<b>Net Cost of Operations With the Public</b>	<b>33,093,214</b>
<b>Net Cost of Operations - Goal Two</b>	<b>\$ 38,325,786</b>

## FY 2004 PERFORMANCE AND ACCOUNTABILITY REPORT

*Goal Three: Ensure market integrity in order to foster open competitive, and financially sound markets*

	<b>Unaudited</b>
Intragovernmental Gross Costs	\$ 3,621,020
Less: Earned Revenue	(8,934)
<b>Intragovernmental Net Cost of Operations</b>	<b>3,612,086</b>
Gross Costs With the Public	22,852,109
Less: Earned Revenue	(7,610)
<b>Net Cost of Operations With the Public</b>	<b>22,844,499</b>
<b>Net Cost of Operations - Goal Three</b>	<b>\$ 26,456,585</b>
 <i>Grand Total</i>	
Intragovernmental Gross Costs	\$ 13,164,472
Less: Earned Revenue	(32,482)
<b>Intragovernmental Net Cost of Operations</b>	<b>13,131,990</b>
Gross Costs With the Public	83,080,452
Less: Earned Revenue	(27,665)
<b>Net Cost of Operations With the Public</b>	<b>83,052,787</b>
<b>Total Net Cost of Operations</b>	<b>\$ 96,184,777</b>

The Statement of Changes in Net Position presents the accounting items that caused the net position section of the balance sheet to change since the beginning of the fiscal year.

	<b>(Unaudited)</b>	
	<b><u>Cumulative Results of Operations</u></b>	<b><u>Unexpended Appropriations</u></b>
<b>Balances, October 1, 2003</b>	<b>\$ (2,957,781)</b>	<b>\$23,550,666</b>
<b>Budgetary Financing Sources</b>		
Appropriations:		
Received	-	90,435,000
Less: Rescinded	-	(533,567)
Less: Canceled	-	(339,153)
Used to Acquire and Provide Services	90,084,561	(90,084,561)
<b>Other Financing Sources:</b>		
Imputed Financing Sources	3,858,871	-
Total Financing Sources	93,943,432	(522,281)
Net Cost of Operations	(96,184,777)	-
<b>Balances, September 30, 2004</b>	<b><u>\$ (5,199,126)</u></b>	<b><u>\$23,028,385</u></b>

#### Budgetary Issues

The FY 2004 Commission budget of \$89.9 million (appropriation less rescissions) was allocated among the following programs:

- ❖ **\$17.7 million for Market Oversight.** The primary responsibility of the Division of Market Oversight (DMO) is to foster markets that accurately reflect the forces of supply and demand for the underlying commodity and are free of abusive trading activity. DMO helps ensure that the markets are performing the vital economic functions of price discovery and risk transfer by monitoring the markets to detect and protect against price manipulation and abusive trading practices DMO also reviews products listed by exchanges and rules and rule amendments submitted by exchanges, and develops, implements, and interprets regulations that are designed to protect the economic functions of the markets, protect market participants, and prevent trading abuses.
- ❖ **\$11.9 million for Clearing and Intermediary Oversight.** The primary responsibility of the Division of Clearing and Intermediary Oversight (DCIO) is to oversee market intermediaries and the self-regulatory programs and compliance activities of the futures industry SROs, which include the U.S. commodity exchanges and the National Futures Association and derivatives clearing organizations. DCIO also is responsible for developing rules to protect market users and financial intermediaries.
- ❖ **\$1.4 million for the Office of the Chief Economist.** The Office of the Chief Economist conducts research on major policy issues facing the Commis-

sion; assesses the economic impact of regulatory changes on the futures markets and other sectors of the economy; participates in the development of Commission rulemakings; provides expert economic support and advice to other Commission divisions; conducts special studies and evaluations; and participates in the in-house training of CFTC staff on matters related to futures, options, swaps, and risk management.

- ❖ \$25.7 million for Enforcement. The Division of Enforcement (DOE) investigates and prosecutes alleged violations of the Commodity Exchange Act and Commission regulations. DOE takes enforcement action against individuals and firms registered with the Commission, those who are engaged in activities that directly or indirectly affect commodity futures and option trading on domestic exchanges, and those who improperly market futures and option contracts.
- ❖ \$2.3 million for the Office of Proceedings. The Office of Proceedings provides an inexpensive, impartial, and expeditious forum for handling customer complaints against persons or firms registered under the CEA. Customers may bring complaints against professionals currently or formerly registered with the Commission if the individuals or firms allegedly violated the antifraud or other provisions of the CEA. Administrative Law Judges (ALJs) or Judgment Officers decide reparations cases. ALJs also decide administrative enforcement cases brought by the Division of Enforcement against firms or persons who have allegedly violated the CEA or Commission regulations.
- ❖ \$5.5 for Office of General Counsel. The Office of the General Counsel (OGC) is the Commission's legal advisor. OGC attorneys represent the Commission in court, appearing regularly before the U.S. courts of appeals and the U.S. district courts in proceedings that involve futures industry professionals. Through its Opinions Program, OGC staff assists the Commission in performing its adjudicatory functions. As legal advisor, OGC reviews all substantive regulatory, legislative, and administrative matters presented to the Commission. OGC also advises the Commission on the application and interpretation of the CEA and other administrative statutes.
- ❖ \$25.4 for Executive Direction and Support. Executive Direction and Support includes the Offices of the Chairman and the Commissioners and the Offices of the Executive Director. The Offices of the Chairman and the Commissioners provide Commission leadership and develops and implements agency policy in furtherance of the purposes of the CEA. The Office of the Executive Director (OED) provides mission support services to the programs of the Commission. OED offices include Financial Management, Human Resources, Information Resources Management, Management Operations and Library. Through these offices, OED provides: strategic planning; resource management; personnel management; financial management; leasing, contracting, and procurement; security and emergency preparedness; information technology resources; and facilities, furniture, and equipment management.

The FY 2004 Commission budget of \$89.9 million was allocated among the following three strategic goals:

\$29.4 to ensure the economic vitality of commodity futures and option markets.

\$35.8 to protect market users and the public.

\$24.7 to ensure market integrity in order to foster open, competitive and financially sound markets.

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# Performance Section

FY 2004 Performance and Accountability Report



## Overview

In its continuing effort to meet the requirements of GPRA and budget and performance integration, the Commission took a fresh look at its strategic performance planning and measurement structure in FY 2004. A team of senior program executives and key managers from OED attended a two-day working session for the purposes of documenting the Chairman's vision of success for the next five years, determining the indicators of success, and how to measure them. The result was a new system that enables the Commission to: 1) allocate FTEs by business process rather than activity; and 2) measure its performance using fewer, more meaningful outcome measures rather than numerous output measures.

In FY 2004, the Commission continues to make progress with respect to each of the standards for success associated with the President's goal of budget and performance integration as outlined below:

- ❖ *Creation, implementation, and monitoring of an integrated performance plan/budget.* With this FY 2006 OMB estimate, the budget request and the Annual Performance Plan have been integrated—with the budget now showing the request broken out by object class, by program, and by strategic goal and planned outcome.

To further demonstrate the Commission's progress, the Budget & Planning and Accounting teams of OFM are working to restructure the financial management system to align the monitoring of spending with that of budgeting or planning for spending. This means a complete overhaul of the Management Accounting Structure Code (MASC) system to better align it with the goals, outcomes, and business processes of the new strategic performance planning and measurement structure.

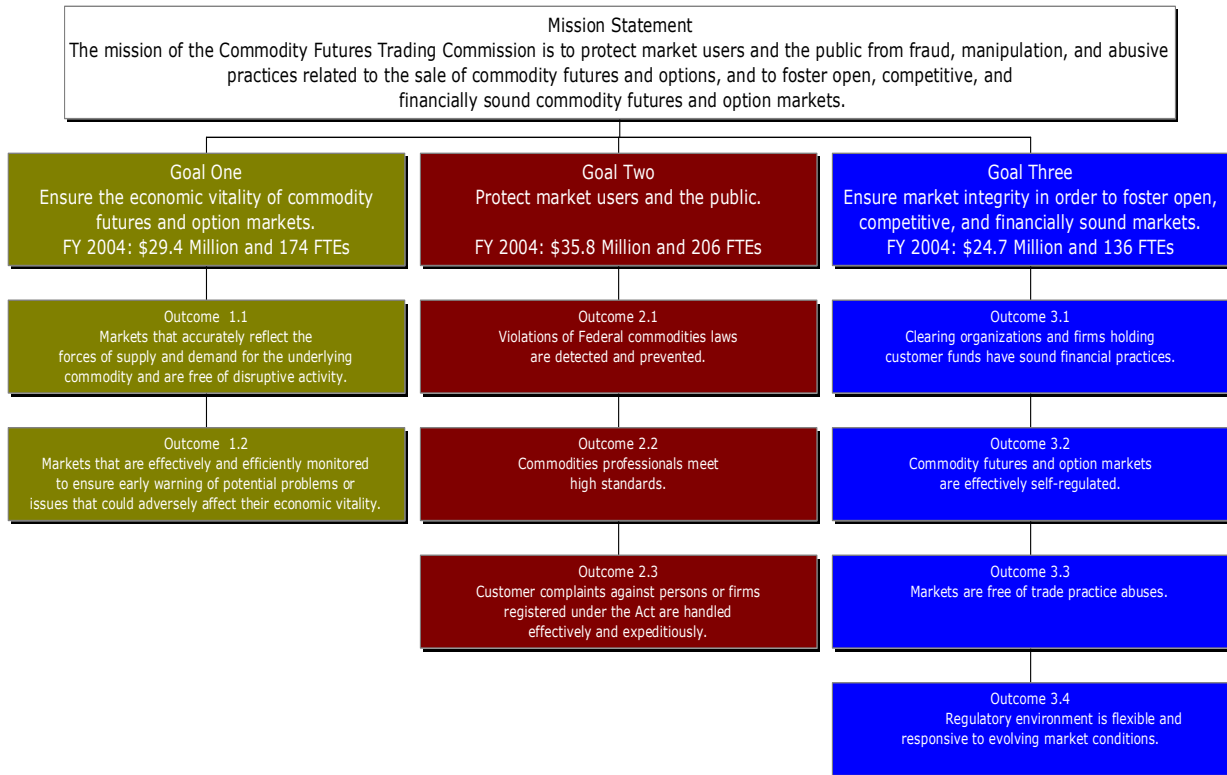
- ❖ *Performance plan/budget sets forth outcome goals, output targets, and requested resources in context of past results.* As mentioned previously, a new strategic planning and measurement structure guided the Commission's latest development of the integrated performance plan and budget. The modifications to the structure were based on input from the Chairman and senior executive staff and evaluations of past performance conducted quarterly by program managers. In addition, the GAO critiqued the Commission's strategic planning structure, providing valuable suggestions regarding how to improve its effectiveness. This year's efforts and these internal evaluations and past critiques have led to a more streamlined set of business processes and performance indicators of success, measures of outcome, and annual performance targets.
- ❖ *Budget accounts, staff, and programs/activities are aligned to achieve program targets.* The work of the Budget & Planning and Accounting teams to restructure budget accounts and the MASC system has enabled a better understanding by program staff of how their activities help the Commission reach its goals, outcomes, and performance targets. As a result, monitoring of resource expenditures—monetary and human—will become more successfully aligned as originally envisioned.
- ❖ *Full cost of outputs and programs is integrated with performance.* The Commission's fully integrated budget and performance estimate contain a cross-cutting analysis that demonstrates how the full cost of each budget request is fully integrated with planned performance. That is, the

program-based and object class-based analyses of the request are augmented by a programmatic distribution of resources by each of the Commission's strategic goals. Conversely, the goal-based analysis of request's planned performance also disaggregates resources by program. This analysis was developed both to demonstrate that full costs were integrated with performance and to engender greater understanding among the public, the Congress, the Administration, market users, and the many other interested persons and entities regarding how resources contribute to the accomplishment of the Commission's mission.

- ❖ Agency documents program effectiveness, analyzes policies' impact on outcomes, and demonstrates how results inform budget decisions. With the work of the senior staff to revamp the strategic performance planning and measurement system as well as the efforts of the Budget & Planning and Accounting teams of OFM to align planning and monitoring of resource expenditure, the Commission will have the foundation in place to begin documenting program effectiveness, analyzing the impact of policy decisions on outcomes, and demonstrating how performance results affect budget decisions.

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## Resource Logic Model



## Goal One

**Strategic Goal One: Ensure the economic vitality of the commodity futures and option markets.**

The focus of this goal is the marketplace. If the U.S. commodity futures and option markets are protected from and are free of abusive practices and influences, they will better operate to fulfill their vital role in our market economy and the global economy—accurately reflecting the forces of supply and demand and serving market users by fulfilling an economic need.

### Outcomes

For Strategic Goal One, in FY 2004 the Commission aimed to achieve these “intermediate” outcomes:

- ❖ Futures and option markets that accurately reflect the forces of supply and demand for the underlying commodity and are free of disruptive activity.
- ❖ Markets that can be used effectively by producers, processors, financial institutions, and other firms for the purposes of price discovery and risk shifting.

The Commission also worked toward these “initial” outcomes:

- ❖ Prevention or mitigation of potentially disruptive situations; and
- ❖ Prevention or mitigation of decreased market use because of a loss of confidence in the integrity of the markets.

## Program Performance Results

### Market Oversight

Monitoring market activity represents one of the ways the Commission seeks to protect the economic functions of the markets. Market Surveillance is conducted to detect attempted manipulation and other abusive practices that could undermine the capacity of these markets to perform their economic function. The Commission takes preventive measures to ensure that market prices accurately reflect fundamental supply and demand conditions, including the routine daily monitoring of large trader positions, futures and cash prices, price relationships, and supply and demand factors in order to detect threats of price manipulation.

In FY 2004, the Market Surveillance subprogram conducted daily surveillance of 556 active futures and option markets. Particularly close monitoring was conducted on the energy futures markets, which experienced periods of high prices and high price volatility due to, among other things, low stocks, geopolitical tension in the Middle East, and strong world economic demand. In addition, very close monitoring was conducted on the cattle futures markets as prices were volatile due to the countervailing pressures of strong demand and the effects of discovery of BSE disease in a single cow in Washington State. The surveillance included collecting and analyzing approximately 35.3 million line items of data regarding large trader activity and approximately 17,035 reports identifying the

large traders. In the course of the year, economists prepared approximately 1,850 weekly surveillance reports and compiled 26 special market reports.

The Market and Product Review staff reviewed three applications of entities seeking to become designated contract markets. The Market and Product Review staff also reviewed five filings by entities that notified the Commission of their intention to operate as exempt markets under the CEA.

The Market and Product Review staff reviewed 16 rule amendment approval requests for existing futures and option contracts in FY 2004. Staff reviewed the terms and conditions of contracts submitted for approval to ensure that the contracts' terms and conditions were in compliance with Commission regulations and policies and did not raise any public interest issues. Under the Commission's certification procedures for listing new products, 204 new contracts were filed, including 29 SFPs, and under its certification procedures, 299 rule changes were filed. Staff reviewed the terms and conditions of contracts submitted under certification procedures to ensure that statutory and regulatory anti-manipulation requirements were met and to provide essential background information in order to conduct market surveillance.

The Commission's review of exchange rules is a key aspect of the statutory framework for self-regulation under Commission oversight. The staff of the Market and Product Review subprogram reviewed exchange rule submissions with a view toward maintaining the fairness and financial integrity of the markets, protecting customers, accommodating and fostering innovation, and increasing efficiency in self-regulation consistent with the Commission's statutory mandates. During FY 2004, staff reviewed 263 exchange rule submissions containing 2,669 separate new rule amendments. The Market and Product Review subprogram is also responsible for providing exemptive, interpretive, or other relief to various markets and market participants to facilitate the continued development of an effective, flexible regulatory environment responsive to evolving market conditions.

#### Clearing and Intermediary Oversight

The Commission's Clearing and Intermediary Oversight program monitors the potential for, and instances of, market disruptions or emergencies related to: 1) the proper capitalization of firms; 2) the proper segregation of customer funds; or 3) issues with respect to systemic risk. Clearing and Intermediary Oversight staff monitor cases of volatile markets in order to advise the Commission of any potential impairment of a registrant or potential systemic risk. It is not possible to estimate in advance the number of such events that will occur annually because market volatility cannot be predicted. Nevertheless, such events are expected to occur. In this connection, Clearing and Intermediary Oversight staff conducted 34 market move reviews in FY 2004. Such reviews met the objectives of: 1) assuring that registrants and financial intermediaries are not impaired by market volatility or disruptions; and 2) detecting any failure to meet clearinghouse obligations or other impairment of a registrant.

#### Enforcement

*Energy Markets.* During FY 2004, the Commission filed a total of 12 enforcement actions in this program area. (See Appendix A)

During FY 2004, the Commission also achieved the following significant litigation result in an action filed in this practice area during the previous fiscal year:

- ❖ *CFTC v. Enron Corp., et al.*, No. H-03-909, Consent Order Of Permanent Injunction And Other Relief Against Defendant Enron Corp. (S.D.Tex. entered May 28, 2004) (energy investigation case filed March 12, 2003; permanent injunction; \$35 million civil monetary penalty). (Thus, the civil monetary penalties imposed in this program area during FY 2004 totaled \$156 million.)

### Office of the Chief Economist

The Office of the Chief Economist performed economic and empirical analyses to evaluate the performance of futures markets and to evaluate the impact of changes in trading rules and in contract specifications on the performance of the futures markets. The office also provided economic and statistical consulting services to Commission staff and offered economic and financial research seminars and short courses in futures, options, and financial economics.

Staff also provided economic and statistical analysis to the Enforcement program on a number of cases involving foreign currencies and energy products and to the Market Oversight program on a review of the need for federal position limits for agricultural futures contracts and on several recently developed derivatives products.

During FY 2004, OCE staff presented research findings relating to price discovery, hedging and market microstructure and development issues at industry or academic conferences as well as through refereed academic journals.

### Office of Proceedings

During FY 2004, the Office of Proceedings continued to hear and decide statutory disqualification actions brought by the Commission.

### Office of the General Counsel

In FY 2004, the Office of the General Counsel (OGC) continued to review for legal sufficiency and for conformance with the CEA and Commission policy and precedent contract market designation applications and applications for registration as derivatives transaction execution facilities (DTEFs) and DCOs.

In FY 2004, OGC continued to advise the Commission concerning implementation of the rules and regulations issued pursuant to the CFMA. OGC has been instrumental in advising the Commission as it comprehensively modernizes the rules governing market intermediaries such as FCMs, CPOs, CTAs and other registrants in light of the study completed by the Commission and submitted to Congress under Section 125 of the CFMA.

OGC also reviewed all proposed enforcement actions alleging manipulation and other abusive trading practices during FY 2004 to assure their legal sufficiency and conformance with Commission policy and precedent.

### Executive Direction & Support

**Administrative Management & Support.** In FY 2004, the Commission's primary mission critical application to support futures and option data market surveillance, the Integrated Surveillance System (ISS), has been significantly enhanced



to address changes and growth in the futures industry. This year those changes included accepting markedly different contract markets that are traded on a new exchange, Hedge Street and daily futures now being traded on the Chicago Mercantile Exchange. In addition, significant effort to improve the capability and availability of the ISS was executed through the implementation of over 12,000 system modifications and the implementation of a second data collection point for transmitted surveillance data to support continuity of operations.

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## Goal One Resources

In FY 2004, the Commission was appropriated \$89.9 million and 516 FTEs, and allocated \$29.4 million and 174 FTEs to Goal One.

**Goal One: Ensure economic vitality of the commodity futures and option markets.**

### Program Funding

	FY 2002 Actual		FY 2003 Actual		FY 2004 Est. Actual	
	\$ (000)	FTE	\$ (000)	FTE	\$ (000)	FTE
Market Oversight	\$9,212	66	\$9,672	70	\$15,631	91
Clearing & Intermediary Oversight	1,000	7	616	4	750	5
Chief Economist	0	0	1,323	7	1,814	13
Enforcement	3,360	23	3,800	23	6,288	36
Proceedings	0	0	0	0	0	0
General Counsel	1,157	7	1,226	7	1,547	11
Executive Direction & Support <sup>1</sup>	6,646	45	8,129	53	3,328	18
<b>TOTAL</b>	<b>\$21,375</b>	<b>148</b>	<b>\$24,766</b>	<b>164</b>	<b>\$29,358</b>	<b>174</b>

<sup>1</sup> Represents Executive Direction resources directly allocated to Goal 1. All unallocated resources are prorated among the other programs.

## Summary of Performance

<b>Goal One: Ensure the economic vitality of the commodity futures and option markets.</b>			
<b>Outcome 1.1: Futures and option markets that accurately reflect the forces of supply and demand for the underlying commodity and are free of disruptive activity.</b>			
<b>Annual Performance Goal:</b> No price manipulation of other disruptive activities that would cause loss of confidence or negatively affect price discovery or risk shifting.			
Performance Measures	FY 2003 Actual	FY 2004 Plan	FY 2004 Est. Act.
Percentage growth in market volume ( <i>Growth in market volume</i> )	22%	TBD	18%
Percentage of novel or innovative market proposals or requests for CFTC action addressed within six months to accommodate new approaches to, or the expansion in, derivatives trading, enhance the price discovery process, or increase available risk management tools ( <i>Expanding Infrastructure</i> )	N/A	N/A	TBD
Percentage increase in number of products traded ( <i>Expanding number of products</i> )	13%	TBD	13%
Percentage of new exchange and clearinghouse applications completed within fast track review period	100%	TBD	100%
Percentage of new contract certification reviews completed within two months to identify and correct deficiencies in contract terms that make contracts susceptible to manipulation	55%	TBD	55%
Percentage of rule change certification reviews completed within two months, to identify and correct deficiencies in exchange rules that make contracts susceptible to manipulation or trading abuses or result in violations of law	64%	TBD	70%
<b>Outcome 1.2: Markets are effectively and efficiently monitored to ensure early warning of potential problems or issues that could adversely affect their economic vitality.</b>			
<b>Annual Performance Goal:</b> To have an effective and efficient market surveillance program.			
Performance Measures	FY 2003 Actual	FY 2004 Plan	FY 2004 Est. Act.
Percentage of DCO applications demonstrating compliance with core principles	100%	100%	100%
Ratio of contracts surveilled per economist	20	TBD	22
Percentage of contract expenditure without manipulation	99.9%	99.9%	99.9%

## Goal Two

### Strategic Goal Two: Protect market users and the public.

The focus of this goal is protection of the firms and individuals—market users—who come to the marketplace to fulfill their business and trading needs. Market users must be protected from possible wrongdoing on the part of the firms and commodity professionals with whom they deal to access the marketplace, and they must be assured that the marketplace is free of fraud, manipulation, and abusive trading practices.

### Outcomes

For Strategic Goal Two, in FY 2004 the Commission aimed to achieve these “intermediate” outcomes:

- ❖ Compliance with federal commodity laws and deterrence of violations.
- ❖ Commodities professionals meet high standards.
- ❖ Customer complaints against persons or firms registered under CEA handled effectively and expeditiously.

The Commission also worked toward these “initial” outcomes:

- ❖ Potential wrongdoing is identified, investigated, and prosecuted.
- ❖ Registered, tested, and licensed commodity professionals.
- ❖ Complaints resolved through settlement, informal voluntary proceedings, or formal adjudicatory proceeding.

### Program Performance Results

#### Clearing and Intermediary Oversight

*Oversight of Sales Practices and Registered Futures Associations.* A core part of the Commission’s mission is to operate a program that protects market users and the public from fraud and abusive practices related to the offer and sale of commodity futures and options. The Clearing and Intermediary Oversight program conducts ongoing oversight related to screening market professionals for fitness and assuring that DCOs have appropriate risk management programs. The Clearing and Intermediary Oversight program also develops disclosure standards, particularly for managed futures and option products, to assure that market users and potential market users are appropriately and consistently informed of the risks of futures and option trading as well as important background information about trading managers.

The Clearing and Intermediary Oversight program oversees the NFA’s Disclosure Document Review program for CPOs and CTAs. Pursuant to a March 2003 delegation of authority by the Commission to the NFA, the program now includes oversight of NFA reviews of disclosure documents filed by CPOs for publicly offered commodity pools. Further, pursuant to a December 2002 delegation of authority by the Commission to the NFA, the program now includes oversight of NFA reviews of annual reports by CPOs for commodity pools that they operate.

Commission staff has frequent contact with NFA staff to coordinate regulatory efforts.

*Oversight of Intermediary Fitness.* In FY 2004, there were 68,948 industry registrants. These registrants included 212 FCMs (16 of which were notice-registered), 1,700 IBs (39 of whom were notice-registered), 1,917 CPOs, and 2,693 CTAs. These firms employ 52,161 sales personnel, known as APs. In addition, there are 8,739 individuals registered as floor brokers (FBs) and 1,526 individuals registered as floor traders executing trades on U.S. exchanges.

The Clearing and Intermediary Oversight program is responsible for performing the Commission's formal oversight of the NFA registration program. This oversight involves inspection of records and interviews with NFA staff as well as numerous informal contacts between NFA and the Clearing and Intermediary Oversight program on a weekly basis. These oversight activities are designed to protect market participants and the public interest by assuring that persons who deal directly with customers and those who handle customer orders and customer funds meet the standards for fitness, integrity, and training established under the CEA. Persons who cannot meet these standards may be subject to statutory disqualification from registration and may have their registration denied, conditioned, or revoked.

The Clearing and Intermediary Oversight program seeks to protect market users and the public by requiring futures industry professionals to meet high standards through registration and passing of a proficiency exam by salespersons. A performance measure established to indicate the percentage of professionals compliant with standards regarding testing, licensing, and ethics training shows that in FY 2004 the program reached 100 percent. When Commission staff uncover persons who are not registered but should be, a letter is sent to the person, and/or the matter is referred for enforcement action.

The Clearing and Intermediary Oversight program chaired the Registration Working Group (RWG), which is composed of Commission and NFA representatives. The RWG was created as a means for the Commission and NFA staff to share ideas and concerns about issues that are not tied to any specific pending registration case. Commission staff participated in four meetings of the RWG during FY 2004, in which the group discussed among other things: 1) registration holds; 2) permitting oral hearings as part of the process of determining whether to suspend a person's registration for willful failure to disclose a criminal matter; 3) the impact of a new Illinois statute on registration under the Act; 4) Rule 30.5 exemptions from Commission registration; and 5) fingerprint processing.

*Anti-Money Laundering.* Clearing and Intermediary Oversight staff worked with representatives of other Commission units and other federal financial regulators on various aspects of a program to combat money laundering and terrorist financing. Specifically, staff worked with Treasury in developing suspicious activity reporting and customer identification rules applicable to FCMs and IBs. The suspicious activity reporting rules apply to transactions occurring after May 18, 2004. Staff also worked with Treasury in developing proposed AML program rules for CTAs, IAs and unregistered investment companies. The final rules are currently being drafted. Staff also worked with the SEC and other agencies in drafting interpretations of the customer identification rules and a proposed no-action position concerning the customers of certain CTAs and IAs. The first tier of the interpretations was issued on June 14, 2004. Staff also continues to work

with Treasury in a process for sharing information about possible terrorists and money launderers. As part of this process, Commission staff maintains and updates a list of FCMs and contact persons, which Treasury then uses when issuing a list of possible money launderers and terrorists on a biweekly basis.

The Major Reviews unit, one of two new units within the Division, was created during FY 2004 to, in addition to managing major risk-focused reviews of exchanges and clearinghouses, develop and review standards for the evaluation and audit of registrant compliance with AML requirements applicable to FCMs, IBs, CPOs, and CTAs.

#### Enforcement

*Forex Cases.* The Commission's work in fighting fraud in FY 2004 continued in the forex trading arena. During FY 2004, the Commission filed a total of 23 enforcement actions in this program area. (See Appendix B)

During FY 2004, the Commission also achieved significant litigation results in 12 actions filed in this practice area during previous fiscal years. (See Appendix B)

*Commodity Pools, Hedge Funds And Commodity Pool Operators.* During FY 2004, the Commission filed six enforcement actions in this program area. (See Appendix B)

During FY 2004, the Commission also achieved significant litigation results in four actions filed in this practice area during previous fiscal years. (See Appendix B)

*Commodity Trading Advisors, Managed Accounts, And Trading Systems.* The Commission filed four enforcement actions in this program area during FY 2004. (See Appendix B)

During FY 2004, the Commission also achieved significant litigation results in two actions filed in this practice area during previous fiscal years. (See Appendix B)

*Introducing Brokers And Their Associated Persons.* During FY 2004, as in past years, the Commission devoted time and attention to matters involving violations by IBs and their APs. Such cases often involve fraudulent misrepresentations, usually to retail customers, to induce them to invest. The Commission has filed two enforcement actions in this practice area during FY 2004. (See Appendix B)

*Futures Commission Merchants.* During FY 2004, the Commission filed one case in this enforcement program area. (See Appendix B)

*Statutory Disqualifications.* During FY 2004, the Commission filed three enforcement actions in this program area. (See Appendix B)

*Quick Strike Cases.* The Commission is committed to responding quickly to enforcement investigations that uncover ongoing fraud. Quick-strike cases are civil injunctive actions that generally are filed in Federal district courts within days or weeks of the discovery of the illegal activity, enabling the Commission to stop fraud at an early stage and to attempt to preserve customer funds. Thus far during FY 2004, the Commission filed 10 quick-strike cases. (See Appendix B)

*Domestic Cooperative Enforcement.* The Commission's cooperative enforcement efforts are an important part of its ability to promote compliance with and deter

violations of Federal commodities laws. Cooperative enforcement enables the Commission to maximize its ability to detect, deter, and impose sanctions against wrongdoers involving U.S. markets, registrants, and customers. The benefits of cooperative enforcement include: 1) the use of resources from other sources to support Commission enforcement actions; 2) coordination in filing actions with other authorities to further the impact of enforcement efforts; and 3) development of consistent and clear governmental responses and avoidance of duplication of efforts by multiple authorities.

As in the past, staff of the Enforcement program have coordinated with numerous Federal, state, and self-regulatory authorities. Historically, program staff have sought assistance from or provided assistance to various Federal agencies, such as the Department of Justice (DOJ), Federal Bureau of Investigation (FBI), SEC, the U.S. Postal Inspection Service, and the Internal Revenue Service (IRS). Similarly, Enforcement program staff have provided assistance to and/or received assistance from state authorities, such as agencies responsible for the regulation of corporations, securities, and banking. The Commission also has provided Federal and local law enforcement authorities with testimony or other assistance in connection with criminal investigations. Enforcement program staff have worked with the DOJ and various U.S. Attorney's offices throughout the Nation, the FBI, the offices of numerous state attorneys general, local police authorities, and task forces focusing on areas such as corporate fraud and forex fraud.

Although the Commission cannot publicly describe the nature of the assistance obtained or given in connection with pending investigations, the following is a sampling of results in cooperative enforcement cases during the past year in which the Enforcement program coordinated its efforts with domestic authorities. These cooperative enforcement cases fall into three general categories: 1) criminal actions in which the Enforcement program provided testimony or other support; 2) matters in which the Commission worked with other criminal or civil authorities and they filed parallel actions; and 3) Commission enforcement actions for which the Commission received assistance from other authorities.

*Other Cooperative Enforcement Efforts.* In addition to direct cooperation with domestic law enforcement and regulatory authorities, the Enforcement program also represents the Commission in a variety of domestic and international efforts, including task forces and working groups designed to keep market participants abreast of new developments in financial crimes and to coordinate governmental responses to common issues. Several examples of the efforts of the Enforcement program in this area follow:

- ❖ *Corporate Fraud Task Force.* By Executive Order signed by President Bush on July 9, 2002, the CFTC was named as a member of the Corporate Fraud Task Force. This task force was established with the objective of strengthening the efforts of DOJ, Federal, state, and local agencies to investigate and prosecute significant financial crimes, recover the proceeds of such crimes, and ensure just and effective punishment of those who perpetrate financial crimes. Recent efforts of this inter-agency cooperative task force have included an investigation of the alleged manipulation of the energy markets during the power crisis of 2000 to 2001.
- ❖ *National Futures Association Assistance.* During FY 2004, the NFA continued to provide invaluable assistance to Commission's Enforcement program in two of its most important program areas: its investigation into the alleged misconduct in the energy markets and its investigation of

forex trading fraud. NFA's assistance included detailing a number of its employees to work shoulder-to-shoulder with Enforcement program staff on these matters. The detailees' expertise, enthusiasm and hard work were an invaluable asset to the Enforcement program and are a proud reflection of the NFA's professionalism and commitment.

- ❖ *Anti-Money Laundering.* The Commission participates in domestic and international AML cooperative enforcement efforts. On the domestic front, the Commission is a member of the Money Laundering Strategy Working Group and the U.S. Treasury Department's Bank Secrecy Act Advisory Group, and Commission staff are consulting with staff of the U.S. Treasury Department in developing regulations as required by the USA PATRIOT Act enacted in response to the terrorist attacks of September 11, 2001. Internationally, the Commission has aided the U.S. delegation to the Financial Action Task Force, including its efforts to combat global terrorist financing.
- ❖ *Telemarketing and Internet Fraud Working Group.* The Telemarketing and Internet Fraud Working Group consists of representatives from state, Federal, and international regulatory and criminal authorities. At the working group's quarterly meetings, members discuss all aspects of telemarketing and Internet fraud, including issues such as new scams, new uses of technology, geographical hotspots for certain types of fraudulent activity, effective enforcement techniques, and recent cases that establish relevant precedent in this area.
- ❖ *Consumer Protection Initiatives Committee.* The Consumer Protection Initiatives Committee was created by the Attorney General's Council on White-Collar Crime to coordinate activities of various agencies' consumer protection programs. Goals of the committee include: 1) minimizing duplication of consumer protection efforts by sharing information on various fraud prevention and enforcement initiatives; 2) developing inter-agency consumer protection initiatives focusing on enforcement, deterrence, and public awareness; and 3) facilitating referrals of cases with strong criminal implications to the DOJ and U.S. Attorney's Offices in order to better address consumer fraud issues.
- ❖ *Securities and Commodities Fraud Working Group.* The Securities and Commodities Fraud Working Group is a vehicle for public and private sector participants to discuss current trends in financial crime in the securities, futures, and option industries and to exchange ideas about enforcement techniques. The group, organized by the Fraud section of the Criminal Division of the DOJ, meets on a quarterly basis, and its members include criminal and regulatory authorities from state and Federal agencies and representatives from various exchanges and other SROs.

#### Office of Proceedings

The Office of Proceedings provides a forum for effectively and expeditiously handling customer complaints against persons or firms registered with the Commission at the time of the alleged wrongdoing or at the time the complaint is filed.

During FY 2004, the Office of Proceedings will meet its goal of resolving most customer complaints within one year from the date the complaint was filed. During FY 2004, 41 percent of the reparations complaints were disposed of within one year from the date the complaint was filed. The remaining complaints were



not resolved within one year as a result of issues beyond the Commission's control. For example, parties requested additional time for one or more of the following reasons: 1) to submit supplementation to their cases; 2) to prepare pleadings; 3) to complete extensive discovery documents; or 4) to deal with personal or professional responsibilities.

The Office of Proceedings' ALJs are responsible for hearing and rendering decisions in administrative enforcement cases brought by the Commission against alleged violators of the CEA or related regulations. The Office of Proceedings decided 45 administrative enforcement cases in FY 2004.

#### Office of the General Counsel

Opinions and Review. Through its Opinions Program, OGC assists the Commission in the performance of its adjudicatory functions. In fulfilling this role, OGC drafts opinions and orders in matters appealed to the Commission. The Commission's jurisdiction in adjudicatory matters includes:

- ❖ Administrative cases prosecuted by the Enforcement program against alleged violators of the CEA or related regulations;
- ❖ Reparations cases brought by customers to recover money damages from industry registrants; and
- ❖ Adjudicatory actions taken by industry SROs.

The Commission issued 24 opinions and orders through the first nine months of FY 2004. Among other decisions, the Commission ruled that a presidential pardon, standing alone, does not nullify a statutory disqualification. The character of a pardoned individual who seeks to be registered remains subject to scrutiny in light of the conduct underlying the disqualification and the pardon. *Hirschberg v. NFA*, Docket No. CRAA-02-03 (CFTC (June 8, 2004) (affirming a decision by the NFA).

The Commission decided two trade practice cases, finding liability against a single respondent in a case involving transactions in gold futures on the Commodity Exchange, Inc., *In re Gorski*, Docket No. 93-5 (CFTC Mar. 24, 2004); and dismissing the complaint against five individuals who traded various futures on three New York exchanges. *In re Fisher*, Docket No. 93-2 (CFTC Mar. 24, 2004).

The Commission also reached divergent results in two cases involving off-exchange transactions in the agricultural market known as "hedge-to-arrive (HTA)" contracts. The Commission held that the HTA contracts in *In re Competitive Strategies, Inc.*, Docket No. 98-4 (CFTC Nov. 23, 2003) were off-exchange, and therefore illegal, futures contracts. It dismissed the complaint against respondents in *In re Grain Land Cooperative*, Docket No. 97-01 (CFTC Nov. 25, 2003), finding that the record did not establish reliably that the transactions were "futures contracts rather than forward contracts" excluded from the CFTC's jurisdiction.

In a third case involving off-exchange contracts used to manage agricultural price risk, the Commission summarily affirmed the initial decision's dismissal of the complaint based on the finding that respondent's "premium offer contracts" were not options, but rather forward contracts excluded from the CFTC's jurisdiction. *In re Cargill*, Docket No. 99-16 (CFTC Nov. 25, 2003).

In FY 2004, OGC assisted with the resolution of appeals from initial decisions in administrative enforcement matters, appeals from initial decisions in reparations matters, and appeals arising out of SRO disciplinary actions.

**Litigation.** Through the litigation program, OGC represents the Commission in the U.S. District Courts and the U.S. Courts of Appeals and assists the Solicitor General in representing the Commission before the U.S. Supreme Court. OGC also monitors litigation of interest to accomplishing the Commission's mission, including the Commission's cooperation with other Federal financial regulators through the President's Working Group on Financial Markets and the President's Corporate Fraud Task Force.

During FY 2004, before the Courts of Appeals, the Commission obtained favorable rulings upon a variety of issues. Most notably, the U.S. Court of Appeals for the Ninth Circuit confirmed the Commission's view of the professional integrity necessary to work as a commodity professional. Specifically, the court affirmed a Commission opinion that held that an individual may be denied a license to work as a CPO or as a CTA if that person has demonstrated a lack of honesty. *CFTC v. Stephen Bronte Advisors*, No. 02-73241 (9<sup>th</sup> Cir.) In another matter, the U.S. Court of Appeals for the Eleventh Circuit affirmed a district court finding of fraud in the retain sale of options contracts. *CFTC v. Matrix Trading Group*, No. 03-13123 (11<sup>th</sup> Cir.).

In a number of cases, the Office of the General Counsel defended cases against violators of the CEA who failed to return funds to defrauded customers, among them, *CFTC v. Heffernan*, No. 03-14494D (11<sup>th</sup> Cir.), *CFTC v. Kingsfield*, No. 03-2413 (4<sup>th</sup> Cir), and *CFTC v. Wall Street et al.*, No. 04-3131 (10<sup>th</sup> Cir.). In addition, on behalf of the Commission, OGC affirmatively sought review before the U.S. Court of Appeals for the Seventh Circuit of the core jurisdictional issue regarding the definition of a futures contract. *CFTC v. Zelener*, No. 03-4245 (7<sup>th</sup> Cir.).

Before the U.S. District Courts, the Office of the General Counsel successfully defended the Commission's right to decide, subject only to appellate review, whether or not an individual has the requisite qualifications to serve as a FB in the commodities industry. *Hirschberg v. CFTC*, 2003 WL 22019310 (N.D.Ill.). In addition, the OGC represented the Commission in personnel cases before the district courts, and before administrative agencies, such as the Equal Employment Opportunity Commission and the Merit Systems Protection Board and represented the Commission in contract matters before the General services Board of Contract Appeals.

The Office of the General Counsel also monitors bankruptcy cases involving futures industry professionals and, as appropriate, assists courts, trustees, and customers in implementing special Bankruptcy Code provisions that pertain to commodity firms. In FY 2004, the Office of the General Counsel appeared before various Bankruptcy Courts throughout the country to protect both the Commission's interest in recovering penalties owed due to market misconduct and the interest of public customers in having their funds recovered and returned. Most notably, during FY 2004, OGC appeared in bankruptcy proceedings involving several firms alleged to have engaged in misconduct in the energy markets. *In re Enron Corp*, No. 01-16034 (S.D.N.Y.); *In re NRG Energy Inc.*, No. 03-13024 (S.D.N.Y.).

Finally, through its *amicus curiae* program, the Office of the General Counsel supports the Commission in assisting the courts in resolving difficult or novel questions arising under the CEA or Commission regulations with the intent of

making significant contributions to the development of consistent and accurate legal precedent. In FY 2004, the Office actively considered participating as *amicus curiae* in one such case.

*Regulatory and Legislative Matters.* In FY 2004, OGC continued to advise the Commission concerning the implementation of rules and regulations issued pursuant to the CFMA. OGC assisted the Commission in new regulatory initiatives to further carry out CFMA mandates, including providing regulatory relief to market intermediaries as contemplated by the CFMA, such as amendments to Part 4 of the Commission's regulations governing the registration and activities of CPOs and CTAs.

OGC, working in conjunction with other programs of the Commission, consulted with staff of the U.S. Treasury Department and various Federal financial regulators to develop AML regulations required under the USA PATRIOT Act, including in FY 2004, a final rule requiring FCMs and IBs to report suspicious transactions. OGC also coordinated the Commission's continuing work with Treasury regarding a number of other regulations required by the USA PATRIOT Act that will impact the futures industry, including: 1) final rules requiring commodity pools, CPOs, CTAs, and securities investment advisers to establish AML compliance programs; and 2) final rules involving correspondent and private banking accounts for non-U.S. institutions and individuals. During FY 2004, OGC also actively participated in an inter-agency working group lead by the Treasury Department to develop and issues guidance concerning the application of the recent customer identification program rules to the futures industry and other sectors of the financial services industry.

Because many hedge fund complexes include registered CPOs and CTAs, OGC has made the Commission's hedge fund information available to the SEC in connection with its ongoing study of that industry. Also, during FY 2004, the General Counsel presented Commission testimony, including extensive hedge fund statistical data and related materials, at a hearing of the Senate Committee on Banking, Housing, and Urban Affairs on "Regulation of the Hedge Fund Industry."

#### Executive Direction & Support

*Administrative Management & Support.* In FY 2004, the Commission began work on Project eLaw, an effort that provides law office automation and modernization to the Division of Enforcement, Office of the General Counsel, and Office of Proceedings. Project eLaw is a Commission-wide initiative that seamlessly integrates technology and work processes to support managers and staff across the Commission in their investigative, trial, and appellate work. Detailed planning and careful execution of Project eLaw tasks required extensive collaboration across the Commission to ensure all internal stakeholders had an opportunity to articulate their needs in this effort. In FY 2004, the requirements analysis, technology assessment, security plan and business impact analysis study were completed.

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## Goal Two Resources

In FY 2004, the Commission was appropriated \$89.9 million and 516 FTEs, and allocated \$35.8 million and 206 FTEs to Goal Two.

Goal Two: Protect market users and the public.

## Program Funding

	FY 2002 Actual		FY 2003 Actual		FY 2004 Est. Actual	
	\$ (000)	FTE	\$ (000)	FTE	\$ (000)	FTE
Market Oversight	\$00	0	\$00	0	\$00	0
Clearing & Intermediary Oversight	2,201	15	2,328	14	6,873	35
Chief Economist	0	0	0	0	0	0
Enforcement	14,955	100	16,229	97	22,121	129
Proceedings	2,000	14	2,256	13	2,732	18
General Counsel	2,563	16	2,930	15	3,815	22
Executive Direction & Support <sup>2</sup>	7,221	47	8,040	48	289	2
<b>TOTAL</b>	<b>\$28,940</b>	<b>192</b>	<b>\$31,783</b>	<b>187</b>	<b>\$35,830</b>	<b>206</b>

<sup>2</sup> Represents Executive Direction resources directly allocated to Goal 2. All unallocated resources are prorated among the other programs.

## Summary of Performance

<i>Goal Two: Protect market users and the public.</i>			
<b>Outcome 2.1: Violations of Federal commodities laws are detected and prevented.</b>			
<b>Annual Performance Goal:</b> Violators have a strong probability of being detected and sanctioned.			
<b>Performance Measures</b>	<b>FY 2003 Actual</b>	<b>FY 2004 Plan</b>	<b>FY 2004 Est. Act.</b>
Number of enforcement investigations opened during the fiscal year	172	120	120
Number of enforcement cases filed during the fiscal year	64	60	60
Percentage of enforcement cases closed during the fiscal year in which the Commission obtained sanctions (e.g., civil monetary penalties, restitution and disgorgement, cease and desist orders, permanent injunctions, trading bans, and registration restrictions)	100%	100%	99%
Cases filed by other criminal and civil law enforcement authorities during the fiscal year that included cooperative assistance from the Commission	19	20	20
<b>Performance Measures</b>	<b>FY 2003 Actual</b>	<b>FY 2004 Plan</b>	<b>FY 2004 Est. Act.</b>
Percentage of SROs that comply with core principles	100%	New	100%
Percentage of DCOs that comply with core principles	100%	100%	100%
Percentage of professionals complaint with standards regarding testing, licensing, and ethics training ( <i>Professional compliance</i> )	100%	100%	100%
Percentage of SROs that comply with requirement to enforce their rules	100%	100%	100%
Percentage of total requests receiving CFTC responses for guidance and advice	93%	90%	90%
<b>Outcome 2.3: Customer complaints against persons or firms registered under the Act are handled effectively and expeditiously.</b>			
<b>Annual Performance Goal:</b> Customer complaints are resolved within one year from the date filed and appeals are resolved within six months.			
<b>Performance Measures</b>	<b>FY 2003 Actual</b>	<b>FY 2004 Plan</b>	<b>FY 2004 Est. Act.</b>
Percentage of filed complaints resolved within one year of the filing date	66%	50%	50%
Percentage of appeals resolved within six months	50%	35%	35%

## Goal Three

**Strategic Goal Three: Ensure market integrity in order to foster open, competitive, and financially sound markets.**

The third goal focuses on several important outcomes—effective self-regulation; firms and financial intermediaries have sound business, financial and sales practices; and responsive and flexible regulatory oversight.

### Outcomes

For Strategic Goal Three, in FY 2003 the Commission aimed to achieve these “intermediate” outcomes:

- ❖ Ensure sound financial practices of clearing organizations and firms holding customer funds.
- ❖ Promote and enhance effective self-regulation of the commodity futures and option markets.
- ❖ Facilitate the continued development of an effective, flexible regulatory environment responsive to evolving market conditions.
- ❖ Promote markets free of trade practice abuses.

The Commission also worked toward these “initial” outcomes:

- ❖ No loss of customer funds as a result of failure of firms to adhere to regulations.
- ❖ No customer prevented from transferring funds from a failing firm to a sound firm.
- ❖ No customer funds lost as a result of failure of an SRO to ensure compliance with its rules.
- ❖ Regulatory reform that is responsive to evolving markets conditions.
- ❖ Prevention and mitigation of trade practice abuses in the market.

## Program Performance Results

### Market Oversight

In FY 2004, Market Oversight’s Market Compliance subprogram staff completed three rule enforcement reviews of SRO compliance programs. Periodic review of self-regulated organization compliance programs is a component of the program’s oversight activity to promote and enhance effective self-regulation and ensure that SROs enforce compliance with their rules.

One of the rule enforcement reviews completed during FY 2004 was a review of the Coffee, Sugar and Cocoa Exchange’s (CSCE’s) audit trail, trade practice surveillance, disciplinary and dispute resolution programs. Market Compliance staff found that CSCE maintains adequate programs with respect to the areas reviewed, but made recommendations to further improve CSCE’s trade practice surveillance and disciplinary programs. Staff recommended that CSCE modify its procedures for monitoring cross trades and impose consistently meaningful sanc-

tions in cases involving similar substantive trading abuses. Market Compliance staff also conducted a review of the New York Mercantile Exchange's (NYMEX's) trade practice, audit trail, disciplinary, and dispute resolution programs. In its review, staff found that NYMEX maintains adequate programs in these areas, and made recommendations to further improve certain aspects of its disciplinary program. Finally, staff conducted a review of the Minneapolis Grain Exchange's (MGE) market surveillance, trade practice surveillance, audit trail, disciplinary, and dispute resolution programs. Similarly, staff found that MGE maintains adequate programs in these areas and made recommendations for further improvement.

The Commission's review of exchange rules is a key aspect of the statutory framework for self-regulation. Market and Product Review subprogram staff review exchange rule submissions with the goals of: 1) maintaining the fairness and financial integrity of the markets; 2) protecting customers; 3) accommodating and fostering innovation; and 4) increasing efficiency in self-regulation consistent with the Commission's statutory mandates. To these ends, the Market and Product Review staff reviewed 263 exchange rule submission packages and, within those packages, staff reviewed 2,669 new rules and rule amendments.

Market and Product Review subprogram staff also work to facilitate industry innovations and new trading methods and market structures, thereby meeting the Commission's objective of promoting and enhancing effective self-regulation and competition. During FY 2004, staff were involved in a number of significant matters including issues related to new exchanges and exempt markets, exchange mergers, novel trading procedures, and new automated trading systems.

#### Issuing Exemptive, Interpretive, and No-Action Relief

The Market and Product Review subprogram is responsible for providing exemptive, interpretive, or other relief to facilitate the continued development of an effective, flexible regulatory environment responsive to evolving market conditions. For example, in FY 2004, the Market and Product Review subprogram issued an interpretative letter to the Australian Wheat Board (AWB) which found that AWB's proposal to have its wholly-owned subsidiary, AWB (USA), Inc., conduct over-the-counter trading, both as an offeror and an offeree of agricultural trade option contracts, fell within the exemptive provisions of regulation 32.13(g). The Commission continued the policy initiated in FY 1999 of issuing no-action letters in response to requests by foreign boards of trade to permit placement of electronic terminals in the U.S. without requiring contract market designation for those boards of trade. In FY 2004, the Market and Product Review subprogram issued a no-action letter to the European Energy Exchange and issued amended no-action letters to Eurex Deutschland and Eurex Zurich, Ltd., to permit, subject to Commission approval, the clearing of Euro products traded on the two exchanges to be cleared by the Clearing Corporation as a special clearing member of Eurex Clearing AG. In FY 2004, the Market and Product Review subprogram also issued an amended no-action relief letter to the Sydney Futures Exchange (SFE) to permit non-clearing SFE members that carry U.S. customer accounts to place SFE terminals with those customers conditioned on the non-clearing member giving up those trades to a guaranteeing FCM or rule 30.10 firm.

#### Clearing and Intermediary Oversight

*Fostering Sound Business Practices: Oversight of SROs, Market Intermediaries, and DCOs.* A key aspect of assuring effective self-regulation is oversight by the



Commission of SRO programs to assure compliance by their members with customer and market protection standards. Toward this end, the Clearing and Intermediary Oversight program oversees, reviews, and reports to the Commission concerning statutorily required self-regulatory programs directed at maintaining the financial integrity of the markets and deterring improper sales practices and other wrongful conduct.

The Clearing and Intermediary Oversight program staff conduct a financial surveillance and audit program that buttresses periodic audit, daily financial surveillance, and other self-policing programs administered by the exchanges and NFA to promote and enhance effective self-regulation of the commodity futures and option markets. The objective of this program is to assure sound financial practices of clearing organizations and firms holding customer funds. The effort includes oversight of financial compliance programs of SROs and direct quality control audits to assess the efficacy of their programs. The oversight of SRO programs is necessary to ensure that SRO member firms are properly capitalized, maintain appropriate risk management capabilities, and that customer funds are held in segregation by appropriate custodians and are protected from misappropriation.

This oversight function of the Clearing and Intermediary Oversight program has taken on increased importance under the Commission's new regulatory framework under the CFMA. The CFMA defined a new category of registered entity, DCOs, and set forth certain core principles governing such entities. Staff also have developed a program for conducting oversight of DCO compliance and have met separately with each DCO to discuss the nature and content of this oversight program.

Similar to the approach of other federal financial regulators and certain overseas financial supervisors, - indeed, in close consultation with several such peers, - the Division has begun to enhance its supervision of exchanges, clearinghouses, and other SROs with risk-based examination cycles and risk-focused reviews. Both the scheduling and scope of the Division's supervisory reviews will now be based on careful analysis of the underlying risks to which an institution is exposed and the controls which it has in place to address those risks. This approach promises to better utilize supervisory resources and to help ensure even greater financial integrity and risk management within the firms and clearinghouses that are the backbone of the futures clearing system.

The Major Reviews unit, one of two new units within the Division, was created during FY 2004 to plan, coordinate, schedule, monitor, and assess major risk-focused reviews. The unit's activities are intended to ensure that multiple, simultaneous major reviews are completed on schedule, follow appropriate benchmarks of consistency and comparability, and, ultimately, provide meaningful assessments of core principle compliance which, when presented formally to the Commission, permit the Commissioners to assure themselves that the Commission is fulfilling its responsibilities on this important aspect of market oversight.

The Clearing and Intermediary Oversight program staff completed six audits (one exchange clearinghouses and five FCMs) in FY 2004 to test compliance with the Commission's financial requirements for the safekeeping of customer funds. In addition, program staff processed 4,671 financial reports filed by registrants. As a result of ongoing program efforts such as these, no regulated customer funds were lost in FY 2004, thereby meeting the program's objective of ensuring sound financial practices of clearing organizations and firms holding customer funds.



*Ensuring a Flexible and Responsive Regulatory Environment.* In FY 2004, the Clearing and Intermediary Oversight program supported the Commission's ongoing regulatory reform program, as well as actions required by or appropriate to the implementation of the CFMA. In February 2004, the Commission amended its rules to further expand the range of permissible investments by FCMs and clearinghouses of their customers' funds and property, which will now be permitted to enter into repurchase agreements and collateral management programs using customer-deposited securities. In April 2004, Clearing and Intermediary Oversight staff issued a letter clarifying application of the CPO exemption that was adopted in August 2003 as Rule 4.13(a)(3). The letter stated that a CPO claiming registration exemption under Rule 4.13(a)(3) may admit Non-United States persons (as defined in Rule 4.7) as participants in the CPO's pool *without* regard to whether such Non-United States persons meet the investor qualifications set forth in Rule 4.13(a)(3)(iii). In light of the Staff Letter, staff developed an amendment to Rule 4.13(a)(3), adopted by the Commission in July 2004, that provides that if a person can participate in a Rule 4.13(a)(4) pool, which has no trading restrictions, it similarly should be able to participate in a Rule 4.13(a)(3) pool, which does have a trading restriction.

*Exemptive, Interpretive, and No-Action Relief.* The Clearing and Intermediary Oversight program is responsible for providing exemptive, interpretive, or other relief to facilitate the continued development of an effective, flexible regulatory environment responsive to evolving market conditions. The Clearing and Intermediary Oversight program responded to a high number of formal and informal requests for guidance concerning the application of regulatory requirements to specific transactions, new products, and market circumstances. Staff issued 176 responses to written requests, including electronic responses, from members of the public and the regulated industry to provide guidance concerning the application of Commission rules and to provide exemptions. The average response time was five weeks. Staff also responded to more than 1,750 telephone inquiries concerning the application of Commission requirements to commodity professionals. These responses aided market participants and the public by providing guidance concerning the manner in which they may conduct their activities to comply with relevant requirements and by granting relief from requirements where application of the rules would not serve the public interest.

The Commission also furthered the development of the foreign futures and option transactions (U.S. customers trading on non-U.S. markets) in FY 2004. The Commission issued an order to the U.K. Financial Service Authority (FSA) consolidating and updating the relief set forth in prior orders issued pursuant to Commission Rule 30.10, reflecting the substitution of the FSA for various U.K. regulatory and SROs and revising certain staff no-action letters regarding the treatment of customer funds attributable to trading on the London Metals Exchange. Among other things, the Commission's order exempted firms designated by the FSA from compliance with the Commission's risk disclosure requirements as they apply to transactions under Part 30, and authorized such firms to permit U.S. customers that are eligible contract participants to opt out of segregation with respect to foreign futures and options transactions. Conference calls were conducted with representatives of each of the foreign exchanges that are recipients of Rule 30.10 relief to update information about contact persons, regulatory reform and structural changes at each exchange, and the accuracy of NFA's list of Rule 30.10 firms at each foreign exchange. These calls also solicited comments from the Rule 30.10 foreign exchanges about any need for amendments to their respective Rule 30.10 orders.

*Security Futures Products and Cooperation with the SEC.* The CFMA also directs the Commission and the SEC to implement a joint regulatory framework for SFPs and narrow-based stock index futures. As part of the ongoing security futures product supervisory and oversight process, the Commission and the SEC signed MOU to clarify the ability of each agency to conduct inspections of notice-registered intermediaries, exchanges, and limited purpose national securities associations. The MOU provides that the CFTC and SEC will notify each other of any planned examinations, advise the other of reasons for an intended examination, provide each other with examination-related information, and conduct examinations jointly, if feasible. The agencies will notify each other of significant market issues and will share trading data and related market information.

The Clearing and Intermediary Oversight program permitted NFA to postpone indefinitely updating the Series 3 and Series 30 examinations to include questions on SFPs. Staff has discussed with NFA and National Association of Securities Dealers how to accomplish eventual updating of the examinations, but, for the time being, salespersons will be permitted to continue to offer SFPs following the taking of a web-based training module. The SEC is in accord with this approach.

#### Enforcement

*Trade Practice.* During FY 2004, the Commission filed two enforcement actions in this program area. (See Appendix C)

*International Cooperative Enforcement.* The Commission continues to coordinate enforcement activities with foreign authorities. During FY 2004 (October 1, 2003 to July 13, 2004), the Commission made 93 requests for assistance to 45 foreign authorities, and it received 23 requests from authorities in foreign jurisdictions. The number of requests made to and received from foreign authorities in FY 2004 have already exceeded the number of requests for the entire FY 2003. In particular this year, the Commission was successful in obtaining assistance, including bank records, in several jurisdictions where we did not have prior cooperative relationships.

Enforcement also has devoted time and resources to matters involving allegations that persons or entities have committed fraud or other misconduct in their cross-border activities. Such misconduct can adversely affect U.S. firms as well as customers located in the U.S. and overseas. The Commission's efforts in this area during FY 2004 included the filing of 15 enforcement actions. (See Appendix C)

*Information-Sharing Arrangements.* The Commission's international information-sharing arrangements enable the Commission and foreign authorities to engage in the bilateral sharing of information to assist each other in the investigation of potential wrongdoing that extends beyond their respective borders.

- ❖ *Statement of Intent - Irish Financial Services Regulatory Authority.* On March 17, 2004, the Commission and Irish Financial Services Regulatory Authority (IFSRA) signed a Statement of Intent (SOI) Concerning Consultation and Cooperation in the Administration and Enforcement of Futures Laws. The SOI provides a framework for information sharing, thereby facilitating cooperation in cross-border investigations of potential violations of commodity futures and options laws. The Commission's arrangement with the IFSRA is the 23rd formal bi-lateral arrangement that the Commission has entered into for enforcement information sharing with its counterparts in other countries.

❖ IOSCO Multilateral Memorandum of Understanding. During FY 2004, the Commission continued its work on the IOSCO Multilateral Memorandum of Understanding Concerning Consultation, Cooperation and the Exchange of Information (MMOU). The MMOU is an important and meaningful undertaking for regulators to expand cooperation by establishing specific minimum standards for securities and futures regulators in the area of information sharing. There are 26 MMOU signatories, including nine foreign authorities that the Commission did not have an information-sharing arrangement with previously.

International Organization of Securities Commissions (IOSCO)

❖ Screening and Approving MOU Applicants. Enforcement program staff along with three other foreign regulators as members of a MMOU Verification Team evaluated the applications of five IOSCO members to become signatories to the MMOU. The Commission also is a member of the Screening Group which makes recommendations to a decision making body of IOSCO concerning whether to accept or reject specific MMOU applications. In FY 2004, the Screening Group reviewed approximately 10 applicants for the MMOU.

❖ Client Identification Task Force. The Enforcement program staff participated in the IOSCO Task Force on Client Identification to determine a range of acceptable options for client identification in the securities and futures industry. The Task Force's work resulted in IOSCO's publication in May 2004 of its *Principles On Client Identification And Beneficial Ownership For The Securities Industry*.

❖ Standing Committee 4. During FY 2004, Enforcement program staff also continued to participate in the Standing Committee on Enforcement and Information-Sharing (SC4) of the Technical Committee of IOSCO. SC4 considers issues and formulates recommendations relating to international assistance in the detection, investigation, and prosecution of securities and futures violations.

**Office of Proceedings**

The Office of Proceedings continued to hear and decide administrative enforcement actions brought by the Commission.

**Office of the General Counsel**

OGC continued its review of requests for no-action relief to allow the offer and sale of foreign exchange-traded foreign stock index futures contracts in the U.S. In FY 2004, OGC issued four no-action letters for six of these foreign exchange-traded foreign stock index futures contracts.

During FY 2004, OGC advised the Commission with respect to legislative provisions affecting the Commission that were included in the Conference Report on the Energy Policy Act, H. Rep. No. 108-375. These included proposals to: 1) amend Section 4b of the CEA to provide the Commission with principal-to-principal anti-fraud authority; 2) amend Section 9 of the CEA to clarify the Commission's false reporting authority; and 3) add savings clauses to the Federal

Power Act and the Natural Gas Act to preserve the Commission's exclusive jurisdiction over market futures and options trading data.

OGC staff also continued to participate in IOSCO's Standing Committee 5 (SC5) on Investment Management. During the year, SC5 considered and issued reports on several topics of importance to collective investment vehicles. With respect to AML, OGC also participated in the development of the IOSCO Task Force on Client Identification principles.

#### Executive Direction & Support

Agency Direction. The Agency Direction subprogram, specifically OIA, assists the Commission in the formulation of international policy by: 1) coordinating with foreign regulatory authorities; 2) participating in international regulatory organizations and forums; and 3) providing technical assistance to foreign governmental bodies. In FY 2004, OIA contributed to this effort by:

- ❖ Coordinating Commission activities within IOSCO and its Technical Committee and standing committees, with special focus on issues raised by index products, short-selling, transparency, error trade policies, cross-border activities of intermediaries, outsourcing and compliance functions;
- ❖ Participating in several IOSCO Task Forces, including chairing the IOSCO Implementation Task Force that completed drafting an assessment methodology for the *IOSCO Objectives and Principles of Securities Regulation*, which was adopted by IOSCO, developed an electronic version of the Assessment methodology and instructions to clarify its application and participated in IOSCO seminars in Spain and India explaining the methodology; participating in the IOSCO-CPSS Task Force on Central Counterparties that developed a combined risk management and default procedure recommendations and assessment methodology for central counterparties, which was released as a consultative document by IOSCO and the CPSS; and participating in an IOSCO Chairs' Committee, which examined ways to strengthen capital markets against financial fraud and issues concerning the activities of credit rating agencies;
- ❖ Providing information to the IOSCO Emerging Markets Committee on its approach to detecting and deterring manipulation;
- ❖ Coordinating Commission representation in the Council of Securities Commissions of the Americas, including contributing a paper on the benefits of futures trading to the securitization of small business loans and participating on ways to advance COSRA's regional technical assistance and training initiatives;
- ❖ Providing expertise to the Committee of European Securities Regulators related to their inquiry into acceptable market practices for commodity markets as part of its deliberations on possible expansion of the Investment Services Directive to commodity markets;
- ❖ Participating in the Joint Forum's initiative to develop principles for outsourcing relevant to securities, banking and insurance firms;
- ❖ Providing assistance to the Financial Sector Assessment Program of the World Bank and International Monetary Fund;
- ❖ Coordinating the development of an arrangement for regulatory cooperation, consultation and the provision of technical assistance with the Securities Exchange Board of India.

- ❖ Coordinating the Commission's provision of representations and regulatory information to regulatory authorities in Australia, Austria, Germany, Italy, the Netherlands, Spain and Switzerland that supported the recognition of three U.S. futures exchanges electronic trading systems and provided regulatory information to assist Australian regulators determination to issue a blanket exemption to U.S. FCMs offering wholesale business in Australia;
- ❖ Coordinating the Commission's comments to the U.S. Treasury Department on various position papers including U.S.-India and U.S.-China dialogue;
- ❖ Organizing the annual meeting for international regulators during the Futures Industry Association conference, focusing on international regulatory approaches to governance and self-governance of organized markets;
- ❖ Participating in and advising the Toronto Centre on leadership with respect to securities and derivatives sector programs;
- ❖ Responding to requests from domestic and international financial regulators for information on the Commission's program and commenting on various reports;
- ❖ Obtaining fitness information from foreign regulators to support the NFA's registration program and responding to requests from foreign regulators for fitness information on Commission registrants that resulted in recognition of US intermediaries abroad;
- ❖ Assisting NFA in designing its Regulatory Alert System, which provides regulatory information on Commission registrants to participating regulators;
- ❖ Providing technical assistance to foreign regulators in FY2004 through visits with staff at the Commission by 89 foreign persons representing 14 foreign jurisdictions, two on-site visits by Commission staff to foreign jurisdictions, and a week-long seminar in Chicago that examined the techniques used to promote market, firm, and customer protections. Sharing this information enhances the knowledge of other regulators and facilitates the development of high levels of global regulatory protections. In FY 2004, 64 persons representing 25 regulatory and market authorities from 44 jurisdictions attended the seminar.

*Administrative Management & Support.* In FY 2004, the Commission implemented a new system, Stressing Positions at Risk (SPARK) that can analyze the financial positions of trading firms in relation to changing market conditions. This application was developed to perform analysis of existing market conditions and conduct "what if" analyses on future changes in support of financial oversight and risk analysis of the futures market.

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## Goal Three Resources

In FY 2004, the Commission was appropriated \$89.9 million and 516 FTEs, and allocated \$24.7 million and 136 FTEs to Goal Three.

**Goal Three: Ensure market integrity in order to foster open, competitive, and financially sound markets.**

## Program Funding

	FY 2002 Actual		FY 2003 Actual		FY 2004 Est. Actual	
	\$ (000)	FTE	\$ (000)	FTE	\$ (000)	FTE
Market Oversight	\$288	2	\$7,316	41	\$7,443	43
Clearing & Intermediary Oversight	12,764	88	7,563	47	7,652	43
Chief Economist	0	0	167	1	0	0
Enforcement	3,333	22	3,758	22	4,870	29
Proceedings	143	1	162	1	207	1
General Counsel	1,060	7	1,201	7	1,787	8
Executive Direction & Support <sup>3</sup>	7,390	49	8,730	51	2,777	12
<b>TOTAL</b>	<b>\$24,978</b>	<b>169</b>	<b>\$28,897</b>	<b>170</b>	<b>\$24,734</b>	<b>136</b>

<sup>3</sup> Represents Executive Direction resources directly allocated to Goal 3. All unallocated resources are prorated among the other programs.

## Summary of Performance

<b><i>Goal Three: Ensure market integrity in order to foster open, competitive, and financial sound markets.</i></b>			
<b>Outcome 3.1: Clearing organizations and firms holding customer funds have sound financial practices.</b>			
<b>Annual Performance Goal:</b> No loss of customer funds as a result of firms' failure to adhere to regulations. No customers prevented from transferring funds from failing firms to sound firms.			
<b>Performance Measures</b>	<b>FY 2003 Actual</b>	<b>FY 2004 Plan</b>	<b>FY 2004 Est. Act.</b>
Lost funds:			
a) Percentage decrease in number of customers who lose funds	0	0	0
b) Amount of funds lost	\$0	\$0	\$0
Number of rulemakings to ensure market integrity and financially sound markets	2	1	1
Percentage of clearing organizations that comply with requirement to enforce rules	100%	100%	100%
<b>Outcome 3.2: Commodity futures and option markets are effectively self-regulated.</b>			
<b>Annual Performance Goal:</b> No loss of funds resulting from failure of self-regulated organizations to ensure compliance with their rules.			
<b>Performance Measures</b>	<b>FY 2003 Actual</b>	<b>FY 2004 Plan</b>	<b>FY 2004 Est. Act.</b>
Percentage of intermediaries who meet risk-based capital requirements	100%	100%	100%
Percentage of clearing organizations that comply with requirement to enforce their rules	100%	100%	100%
<b>Outcome 3.3: Markets are free of trade practice abuses.</b>			
<b>Annual Performance Goal:</b> Minimize trade practice abuses.			
<b>Performance Measures</b>	<b>FY 2003 Actual</b>	<b>FY 2004 Plan</b>	<b>FY 2004 Est. Act.</b>
Percentage of exchanges deemed to have adequate systems for detecting trade practice abuses	100%	100%	100%
Percentage of exchanges that comply with requirement to enforce their rules	100%	100%	100%
<b>Outcome 3.4: Regulatory environment is flexible and responsive to evolving market conditions.</b>			
<b>Annual Performance Goal:</b> TBD			
<b>Performance Measures</b>	<b>FY 2003 Actual</b>	<b>FY 2004 Plan</b>	<b>FY 2004 Est. Act.</b>
Percentage of CFMA Section 126(b) objectives implemented	100%	100%	100%
Number of rulemakings, studies, interpretations, and guidance to ensure market integrity and exchanges' compliance with regulatory requirements	5	4	4
Percentage of requests for no-action or other relief completed within six months related to novel market or trading practices and issues to facilitate innovation	100%	TBD	100%
Percentage of total requests receiving CFTC responses for guidance and advice	93%	90%	90%



## Methodology for Collecting, Maintaining, and Analyzing Performance Data

### Market Oversight

Statistics concerning the large trader and exchange data collection systems are computer-generated based on the number of actual reports processed. Similarly, counts on numbers of markets trading, reports prepared, and new contract and rule change filings analyzed and completed are derived from computer records. Performance data from regional offices and headquarters are collected quarterly and combined into an overall report reflecting performance data included in the Annual Performance Plan. Trends in volume, open interest, and number of contracts approved are used to project workload statistics for future periods. Compliance factors, such as audits and letters to traders and reporting firms, are reviewed in the context of total reports processed for anomalous relationships. The number of market surveillance reports and special reports are viewed in the context of the number of markets trading and analyses that are presented at Commission meetings. These reports and comparisons with indicators from previous periods are used to verify data accuracy.

The Market and Product Review subprogram calculates the performance data included in the Commission's Annual Performance Report and Annual Performance Plan by querying its automated database, the Designation and Rule Tracking (DART) system. Among other pieces of data, the DART system records for each new product and new rule submission information on the date received, the submission's ultimate disposition, the date of disposition, and the processing time.

The Market Compliance subprogram's performance data are continuously collected from regional and headquarters staff and are maintained at headquarters for each performance category. The adequacy of self-regulated organizations' sanctions and a comparison of sanctions across all exchanges is conducted quarterly by regional staff and is also maintained at headquarters.

### Clearing & Intermediary Oversight

Compliance and Registration. The Compliance and Registration subprogram compiles data on discrete events, such as letters written, rules promulgated or revised, and RWG meetings held. It should be noted that statistics on numbers of letters issued or rules promulgated may not reflect the complexity of any particular matter or the resources necessary to address one issue versus another issue.

Audit and Financial Review. Each branch of the Audit and Financial Review subprogram prepares a monthly report that includes statistics for those projects that can be reported on a numerical basis and also describes special projects, enforcement support, and all other noteworthy matters that staff have worked on during the month. Statistical summaries are also prepared on a quarterly basis.

Clearing Policy. The Clearing Policy subprogram maintains an ongoing status report of current and completed projects. Separately, the Commission is close to completion of development of an electronic database to track all exchange and clearinghouse rule filings.



### Enforcement

The performance data reported by the Enforcement program come from a variety of sources. For example, certain basic information—such as the numbers of investigations and cases opened, closed, and pending—is collected and tabulated on a routine basis by staff in the headquarters office. Case status information is then cross-checked on a monthly basis against status reports submitted by staff to the Office of the Director of the Enforcement program. This information is adapted for use in performance reporting (i.e., individual matters are identified by the goals and activities under which they most reasonably fall).

Other data that are routinely tracked and then adapted for use in performance reporting include sanctions assessed in enforcement matters. In enforcement cases, sanctions can be assessed and/or affirmed by: 1) Commission ALJs; 2) the Commission in settlement or on appeal of an ALJ's decision; 3) Federal district courts hearing injunctive matters; 4) Federal circuit courts of appeal on appeals of district court or Commission decisions; and 5) the U.S. Supreme Court on appeals of decisions by circuit courts of appeal. Commission staff in the Enforcement program regularly track these results and monitor them in order to determine when sanctions become final and effective. Program staff receive notice of sanctions assessed either from the Office of Proceedings in administrative actions, from the team conducting the litigation in injunctive actions, or from OGC in actions before circuit courts of appeal.

Finally, additional data tracked by the Enforcement program—particularly data reflecting investigation and litigation tasks—come directly from the headquarters units and regional offices performing the work. Staff from each subprogram and regional office are required to submit monthly status reports on all pending matters. In conjunction with these monthly submissions, staff are required to fill out an electronic form that provides specific information for each matter. While every effort is made to ensure that the data obtained from the investigation and litigation teams is accurate, the integrity of this data is ultimately and primarily the responsibility of the reporting teams.

### Office of the Chief Economist

Assessment of the performance of the Office of the Chief Economist is based upon reports and consultations completed, which are maintained by OCE staff members themselves. The analysis of these performance data considers both the scale and the complexity of the assignments.

### Office of Proceedings

The Office of Proceedings uses “Repcase,” the integrated computerized case tracking system, to collect, maintain, and analyze performance information for each reparations case. The reparations case reports are separated into two sections—complaints and hearings. The data and information collected in the complaints section consists of the number of cases pending the first of the month, the number of cases received during the month, the number of cases disposed of in complaints, and the number of cases pending at the end of the month. The data and information collected for the hearings section consists of the number of cases pending with an ALJ or judgment officer (JO) at the beginning of the month, the number of cases assigned during the month (including remands, reassignments, and motions to vacate), the number and type of cases disposed of during the month, and the number of cases pending with each ALJ or JO at the end of the month.

A separate database, “Docket Book,” is used to track administrative cases, i.e., administrative/enforcement, exchange, statutory disqualification, and Commission review cases. The administrative case tracking system tracks the number of cases received during the month, the number and type assigned during the month, and the number and type disposed of during the month. Case status information is checked on a monthly basis against status reports submitted by the judges, JOs, and proceedings clerk to the director of the Office of Proceedings. This information is adapted for use in performance reporting.

#### Office of the General Counsel

OGC uses Repcase to collect, maintain, and analyze performance information for each reparations, enforcement, exchange review, and NFA case on appeal to the Commission. Statistical data is collected and reported by the total number of: 1) cases resolved (e.g., final disposition, remand, interlocutory disposition, and miscellaneous disposition); 2) matters received (e.g., merits appeals, interlocutory appeals, and miscellaneous); 3) matters pending; and 4) drafts pending before the Commission.

OGC collects and maintains case data on a monthly, quarterly, and annual basis. A legal program assistant uses this information to prepare monthly, quarterly, and annual reports, which are used by management to monitor and analyze all cases on appeal to the Commission.

- ❖ *Bimonthly Report.* At the end of each bimonthly period, the legal program assistant prepares a bimonthly report for the General Counsel’s signature for submission to the Chairman. The information reported includes all activity (i.e., legislative, regulatory, litigation-related, and opinions-related) in the office that occurred during that period.
- ❖ *Monthly Opinions Report.* At the end of each month, the legal program assistant prepares a monthly report for the General Counsel’s signature. The information reported includes all activity (i.e., disposition of cases, matters received, and matters pending) in the Opinions Program that occurred during the month.
- ❖ *Annual Report.* At the end of each fiscal year, the legal program assistant prepares a statistical summary that shows activity in the program during the fiscal year. The report lists by category the number of matters received, Commission orders and opinions issued, and the number of cases pending at the end of the year. All issued opinions and orders are maintained in binders filed alphabetically, monthly, quarterly, and annually.

In preparing these reports, the legal program assistant reviews the statistical data provided by the Repcase tracking system as well as issued opinions and orders maintained in the binders. This staff member also maintains a separate tracking system of the cases on appeal, which serves as a check against the data provided by the automated tracking system. All reports are reviewed and approved by the General Counsel and/or Deputy General Counsel for the Opinions and Review section.

#### Executive Direction & Support

*Office of International Affairs.* OIA developed a new database system that staff uses to file all projects, correspondence and written advice. The filing system uses

a standardized “Main Topic” and “Key word” format that correspond to certain of the performance indicators used in the performance measurement process. When a project is completed, staff members close out the file, record the action in the database, and file a paper copy of the project work product by year and file code number. As a result, the OIA database captures all work products and permits immediate computer-searchable access to the project and to the paper copy. The system also captures a record of arranged visits to the Commission and regional offices by numerous foreign regulators.

Office of Information Resources Management. OIRM acts on the basis of the *CFTC Five-Year Plan for Information Resources Management* and direction from the Executive Management Council. Performance data is collected by comparing the products actually delivered against the products called for in the plan and the resources used to deliver those products as recorded in the Commission time and attendance data or equivalent OIRM internal records for internal FTEs and the Commission’s financial management system or equivalent OIRM internal records for purchased resources. The five-year plan reflects Commission priorities, actual (as opposed to planned) project performance, and the resources that will be made available to OIRM to pursue projects. Analysis of performance data involves comparison of resources expended on projects with the planned expenditures to the products delivered with the products planned.

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## Program Assessment Rating Tool

OMB uses the Program Assessment Rating Tool (PART) to assess federal programs. Through the use of in-depth diagnostic questions, the PART is employed to assess and evaluate programs across a set of performance-related criteria. PART results are then used to help improve program management and ensure that the American taxpayer receives the best value for their tax dollar.

Beginning in the spring of 2004, OMB began review of the Commission's Enforcement program. The review is still in progress. The results of the review will be included in the Commission's FY 2005 Performance and Accountability Report.

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## External Challenges and Factors

### External Challenges and Factors

The Commission faces challenges external to the organization that may significantly alter its ability to meet its mission, goals, and outcomes, depending on the weight of their influence and the timing of their occurrence. There are three broad areas of external challenges that may impact the Commission's achievement of its strategic goals and planned accomplishments for FY 2004 through FY 2009:

#### Challenges in the Marketplace

The continuing growth in the number of actively traded contracts on U.S. exchanges—nearly triple the number available just a decade ago—poses a significant external challenge. In the last decade, 956 new futures and option contracts were approved or certified. In FY 2004 alone, 209 new futures and option contracts were approved or certified. Since the passage of the CFMA, the Commission has designated eight new contract markets and approved five additional DCOs.

Over one billion contracts are now being traded on futures and option exchanges. The CFTC must monitor the increases in volume and the complexity of trading activity in order to ensure that market users are able to trust the safety, fairness, and transparency of trading on U.S. exchanges.

Events that could destabilize commodity markets in particular and financial markets in general, such as attempts to manipulate prices and the loss of investor confidence caused by recent events in the energy and financial sectors, also present significant challenges to the Commission.

#### Legislative Challenges

The Commission's mission performance continues to be affected by changes in Federal laws and policies, such as the deregulation of the energy industry and changes in farm subsidy policies, spawning change and innovation, new types of crop insurance, structural changes permitted in the financial services industry, the diversification into overseas markets and the convergence of the securities, commodities, insurance, and banking industries.

#### Technological Challenges

The advancements in technology continue to introduce challenges in many areas: alternatives to the "open-outcry" method of trading commodity futures on the exchange floor; enhanced methods for timing and tracking trading transactions; online filing of financial information by market users; solicitations to the retail market via the Internet; electronic marketing and trading of financial and risk-hedging products; and trading commodity futures and options on a global, 24-hour real-time basis. The extraordinary increase in electronic trading systems and Internet trading has allowed markets to respond to information and the needs of their users 24 hours a day, but also has presented new opportunities for fraudulent activity.

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# Financial Section

FY 2004 Performance and Accountability Report





## Message from the Acting Chief Financial Officer and Executive Director

In FY 2004, the CFTC made significant progress in improving its financial performance and reporting to comply with the requirements of the Accountability of Tax Dollars Act of 2002. The Act required the CFTC to prepare its first audited financial statements and integrate the results into a Performance and Accountability Report.

Through the hard work and dedication of the financial management, program, and audit staffs, we successfully completed the requirements of preparing financial statements, undergoing audit scrutiny, and producing the results that are published in this Performance and Accountability Report.



I am pleased to present the CFTC's first audited financial statements for FY 2004. Our independent auditor, KPMG LLP, has rendered an unqualified (clean) opinion on the agency's balance sheet. This opinion attests to the fact that the agency's balance sheet presents fairly, in all material respects, the financial position of the CFTC as of September 30, 2004, in conformity with U.S. GAAP.

Because this is the Commission's first independent audit, the scope of the audit did not include fiscal years prior to FY 2004. As a result, the auditors were not able to express an opinion on accompanying statements of net cost, changes in net position, budgetary resources, financing, and custodial activity since these statements are affected by the unaudited amounts as of the beginning of FY 2004.

We are pleased with our initial results and will continue to build on this sound foundation for FY 2005. Through the continued dedication and collaborative efforts of our staff, we will take steps to improve our internal controls, resolve the weaknesses identified in the independent auditors' report, and successfully meet the challenges ahead. We look forward to achieving success in meeting the new reporting requirements for producing interim statements with accelerated due dates, enhancing financial systems to improve functionality and strengthen regulatory compliance, and acquiring an unqualified (clean) audit opinion on our FY 2005 financial statements.

A handwritten signature in black ink, appearing to read 'Madge A. Bolinger', written over a horizontal line.

Madge A. Bolinger  
Acting Chief Financial Officer and Executive Director  
November 17, 2004

*Commodity Futures Trading Commission***Balance Sheet**

As of September 30, 2004

**Assets**

## Intragovernmental:

Fund Balance with Treasury (Note 3)	\$ 26,304,227
Accounts Receivable (Note 4)	22,806
<b>Total Intragovernmental</b>	<b>26,327,033</b>

Custodial Fines and Interest Receivable, Net (Note 4)	35,402,939
Accounts Receivable (Note 4)	9,457
Equipment and Furniture, Net (Note 5)	340,210
Software, Net (Note 5)	149,428

<b>Total Assets</b>	<b>\$ 62,229,067</b>
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**Liabilities**

## Intragovernmental:

FECA Liabilities	\$ 194,102
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## With the Public:

Trade Accounts Payable	1,025,643
Accrued Funded Payroll and Benefits	2,282,462
Annual Leave	4,797,304
Actuarial FECA Liabilities	514,932
Custodial Liabilities	35,402,939
Contingent Liabilities (Note 8)	182,426

<b>Total Liabilities</b>	<b>44,399,808</b>
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Commitments and Contingencies (Notes 7 and 8)

**Net Position**

Cumulative Results of Operations	(5,199,126)
Unexpended Appropriations	23,028,385

<b>Total Net Position</b>	<b>17,829,259</b>
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<b>Total Liabilities and Net Position</b>	<b>\$ 62,229,067</b>
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*The accompanying notes are an integral part of these financial statements.*

*Commodity Futures Trading Commission***Statement of Net Cost (unaudited)**

For the Year Ended September 30, 2004

*Ensure the economic vitality of the commodity futures and options markets*

Intragovernmental Gross Costs	\$ 4,297,937
Less: Earned Revenue	(10,605)
<b>Intragovernmental Net Cost of Operations</b>	<b>4,287,332</b>
Gross Costs With the Public	27,124,106
Less: Earned Revenue	(9,032)
<b>Net Cost of Operations With the Public</b>	<b>27,115,074</b>
<b>Net Cost of Operations - Goal One</b>	<b>\$ 31,402,406</b>

*Protect market users and the public*

Intragovernmental Gross Costs	\$ 5,245,515
Less: Earned Revenue	(12,943)
<b>Intragovernmental Net Cost of Operations</b>	<b>5,232,572</b>
Gross Costs With the Public	33,104,237
Less: Earned Revenue	(11,023)
<b>Net Cost of Operations With the Public</b>	<b>33,093,214</b>
<b>Net Cost of Operations - Goal Two</b>	<b>\$ 38,325,786</b>

*Ensure the market integrity in order to foster open, competitive, and financially sound markets*

Intragovernmental Gross Costs	\$ 3,621,020
Less: Earned Revenue	(8,934)
<b>Intragovernmental Net Cost of Operations</b>	<b>3,612,086</b>
Gross Costs With the Public	22,852,109
Less: Earned Revenue	(7,610)
<b>Net Cost of Operations With the Public</b>	<b>22,844,499</b>
<b>Net Cost of Operations - Goal Three</b>	<b>\$ 26,456,585</b>

*(Continued)*

*Commodity Futures Trading Commission*

## Statement of Net Cost (unaudited), continued

For the Year Ended September 30, 2004

*Grand Total*

Intragovernmental Gross Costs	\$ 13,164,472
Less: Earned Revenue	(32,482)
<b>Intragovernmental Net Cost of Operations</b>	<b>13,131,990</b>
Gross Costs With the Public	83,080,452
Less: Earned Revenue	(27,665)
<b>Net Cost of Operations With the Public</b>	<b>83,052,787</b>
<b>Total Net Cost of Operations</b>	<b>\$ 96,184,777</b>

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*The accompanying notes are an integral part of these financial statements.*

*Commodity Futures Trading Commission*

Statement of Changes in Net Position (unaudited)

For the Year Ended September 30, 2004

	<b><u>Cumulative Results of Operations</u></b>	<b><u>Unexpended Appropriations</u></b>
<b>Balances, October 1, 2003</b>	<b>\$ (2,957,781)</b>	<b>\$ 23,550,666</b>
<b>Budgetary Financing Sources</b>		
Appropriations:		
Received	-	90,435,000
Less: Rescinded	-	(533,567)
Less: Canceled	-	(339,153)
Used to Acquire and Provide Services	90,084,561	(90,084,561)
<b>Other Financing Sources:</b>		
Imputed Financing Sources	3,858,871	-
Total Financing Sources	93,943,432	(522,281)
Net Cost of Operations	(96,184,777)	-
<b>Balances, September 30, 2004</b>	<b>\$ (5,199,126)</b>	<b>\$ 23,028,385</b>

*The accompanying notes are an integral part of these financial statements.*

*Commodity Futures Trading Commission*

## Statement of Budgetary Resources (unaudited)

For the Year Ended September 30, 2004

**Budgetary Resources**

Budget Authority	
Appropriations Received	\$ 90,435,000
Unobligated Balance, Beginning of Year	9,340,776
Spending Authority from Offsetting Collections:	
Reimbursements Earned and Collected	554,529
Receivable from Federal Sources	22,806
Recoveries of Prior Year Obligations	8,902,248
Permanently Not Available:	
Cancellation of Expired Accounts	(339,153)
Enacted Reduction	(533,567)
<b>Total Budgetary Resources</b>	<b>\$ 108,382,639</b>

**Status of Budgetary Resources**

Obligations Incurred, Direct	\$ 106,987,136
Unobligated Balance Apportioned	38,613
Unobligated Balance Not Available	1,356,890
<b>Total Status of Budgetary Resources</b>	<b>\$ 108,382,639</b>

**Relation of Obligations to Outlays**

Obligated Balance, Net, Beginning of Year	<b>\$ 19,713,939</b>
Obligated Balance, Net, End of Year:	
Accounts Receivable	(22,806)
Undelivered Orders	21,623,425
Funded Accounts Payable and Accruals	3,308,105
<b>Total Obligated Balance, End of Year</b>	<b>\$ 24,908,724</b>

**Outlays:**

Disbursements	\$ 92,867,297
Collections	(554,529)
Subtotal Outlays	92,312,768
Less: Offsetting Receipts	(13,541)
<b>Net Outlays</b>	<b>\$ 92,299,227</b>

*The accompanying notes are an integral part of these financial statements.*

*Commodity Futures Trading Commission*

Statement of Financing (unaudited)

For the Year Ended September 30, 2004

**Resources Used to Finance Activities**

Obligations Incurred	\$ 106,987,136
Less: Spending Authority from Offsetting Collections and Recoveries	(9,479,583)
Net Obligations	97,507,553
Other Resources - Imputed Financing from Cost Absorbed by Others	3,858,871
<b>Total Resources Used to Finance Activities</b>	<b>101,366,424</b>

**Resources Used to Finance Items Not Part of the**

**Net Cost of Operations**

Change in Undelivered Orders	(7,483,065)
Resources that Finance the Acquisition of Fixed Assets	(196,857)
<b>Total Resources Used to Finance Items Not Part of the Net Cost of Operations</b>	<b>(7,679,922)</b>

**Resources Used to Finance the Net Cost of Operations**

**93,686,502**

**Components of the Net Cost of Operations That Will Not Require**

**Or Generate Resources in the Current Period**

Increase in Annual Leave and FECA Liabilities	2,364,826
<b>Total Net Cost of Items That Will Generate Resources in Future Periods</b>	<b>2,364,826</b>

**Components Not Requiring or Generating Resources**

Depreciation and Amortization	128,239
Other Adjustments	5,210
<b>Total Components Not Requiring or Generating Resources</b>	<b>133,449</b>

**Net Cost of Operations**

**\$ 96,184,777**

*The accompanying notes are an integral part of these financial statements.*

*Commodity Futures Trading Commission*

## Statement of Custodial Activity (unaudited)

For the Year Ended September 30, 2004

**Revenue Activity****Sources of Cash Collections**

Registration and Filing Fees	\$ 768,130
Fines, Penalties, and Forfeitures	122,468,925
General Proprietary Receipts	13,541

**Total Cash Collections**

123,250,596

**Increase in Accounts Receivable**

35,376,188

158,626,784

**Disposition of Collections**

Transferred to Treasury (123,250,596)

Increase in Custodial Liabilities (35,376,188)

**Net Custodial Activity**

\$ -

*The accompanying notes are an integral part of these financial statements.*



## Notes to Financial Statements

As of and For the Fiscal Year Ended  
September 30, 2004

### Note 1. Reporting Entity

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The Commodity Futures Trading Commission (CFTC) is an independent agency in the executive branch of the federal government. Congress created the CFTC in 1974 under the authorization of the Commodity Exchange Act (CEA) with the mandate to regulate commodity futures and option markets in the United States. The agency's mandate was renewed and expanded under the Futures Trading Act of 1978, 1982, and 1986; under the Futures Trading Practices Act of 1992; and under the CFTC Reauthorization Act of 1995. The CFMA reauthorized the Commission through Fiscal Year (FY) 2005. Since its inception, the CFTC has continuously operated through authorized appropriations. The CFTC is not subject to Federal, state, or local income taxes.

The CFTC is responsible for ensuring the economic utility of futures markets by encouraging their competitiveness and efficiency, ensuring their integrity, and protecting market participants against manipulation, abusive trade practices, and fraud.

### Note 2. Summary of Significant Accounting Policies

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#### Basis of Presentation and Accounting

The financial statements have been prepared to report the financial position and results of operations for the CFTC, as required by the Accountability of Tax Dollars Act of 2002, the Chief Financial Officers' Act of 1990, and the Government Management Reform Act of 1994. They are presented in accordance with the form and content requirements contained in Office and Management and Budget (OMB) Bulletin No. 01-09, "Form and Content of Agency Financial Statements." This is the first year in which the CFTC has been subject to audit; therefore, the financial statements are presented for FY 2004 only.

The financial statements have been prepared from the CFTC's books and records in conformity with accounting principles generally accepted in the United States (U.S.) prescribed for the Federal government by the Financial Accounting Standards Advisory Board, promulgated by the OMB, and the agency's accounting policies as summarized in this note.

The financial statements have been prepared to include the accounts of all funds under CFTC control in the consolidated format required by OMB Bulletin No. 01-09. The financial statements report on the CFTC's financial position, net cost of operations, changes in net position, budgetary resources, financing, and custodial activities of the CFTC. The books and records of the agency served as the source of information for preparing the statements in the prescribed formats. They are prepared in addition to the financial reports used to monitor and control budgetary resources that are prepared from the same books and records. The state-

ments should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

The CFTC's Balance Sheet presents the financial position of the agency. The Statement of Net Cost presents the agency's operating results, the Statement of Changes in Net Position displays the changes in the agency's equity accounts. The Statement of Budgetary Resources presents the sources, status, and uses of the agency's resources and follows the rules for the Budget of the U.S. Government and reports intra-fund entity transactions without elimination. The Statement of Financing presents the reconciliation of the of the agency's use of budgetary resources with its operating results. The Statement of Custodial Activity presents the sources and disposition of collections for which the CFTC is the fiscal agent, or custodian, for the U.S. Treasury's General Fund Miscellaneous Receipt accounts.

Throughout these financial statements, assets, liabilities, earned revenue and costs have been classified according to the type of entity with whom the transactions are with. Intragovernmental asset and liabilities are those from or to other federal entities. Intragovernmental earned revenues represent collections or accruals of revenues from other federal entities and intragovernmental costs are payments or accruals to other entities.

#### Budgetary Resources and Status

The CFTC is funded through the execution of congressionally-approved appropriations, all under Treasury symbol 95-1400. It is responsible for administering the salaries and expenses of the agency through the execution of these appropriations.

Budgetary resources consisted of unobligated balances of resources brought forward from the prior year and new resources in the form of appropriations and collections for services. The balance forward and collections for services are set forth in line items on the Statement of Budgetary Resources.

Permanent indefinite appropriations and collection authority are available for new obligations without further action by the Congress, on apportionment by OMB and allotment by the CFTC. Annual appropriations and collection authority expire after one year. Annual appropriations are available for new obligations during their period of availability and for five years after that to fund net upward adjustments of prior-year obligations, i.e., they are not available for new obligations. The status of resources in which authority is available for new obligations at year-end is called "unobligated authority available." Authority available only to fund net upward adjustments of prior-year obligations at year-end is termed "unobligated authority not available."

After the end of the five-year expiration period, an appropriation authority is canceled and cannot be used for any purpose. All unused monies related to canceled appropriations are returned to Treasury. Canceled authority is reported as a line item on the Statement of Budgetary Resources.

Obligations, or "obligated authority" refer to orders placed for goods and services not yet received, or for benefits to be provided, called "undelivered orders," and for goods and services received, or for benefits provided, called "delivered orders." Undelivered orders may have cash advances with them, although CFTC does not have any undelivered orders with advances. Delivered orders may be either paid or unpaid at the end of the fiscal year.

There are no material differences between the Statement of Budgetary Resources and related budgetary information reported to OMB, or in the Budget of the U.S. Government.

#### Assets

Assets consist of entity and non-entity assets. Entity assets are those assets that the CFTC has authority to use for its operations. Non-entity assets are those held by the CFTC that are not available for its use. All CFTC assets are entity assets except net custodial accounts receivable.

#### Fund Balance with Treasury

Fund Balance with Treasury is the aggregate amount of CFTC's accounts with Treasury for which CFTC is authorized to make expenditures and pay liabilities. CFTC does not maintain bank accounts of its own, has no disbursing authority of its own, and does not have any cash held outside of Treasury. Treasury disburses funds for the agency on demand, and monies collected by CFTC are deposited to the U.S. Treasury. (See Note 3.)

#### Accounts Receivable

Accounts receivable consists of amounts owed by other federal agencies and the public to the CFTC. They are claims for payment as a result of employee repayments, overpayments to vendors, custodial fines, and interest receivable resulting from civil monetary penalties. Accounts receivable are valued net of an allowance for uncollectible amounts. The allowance is based on past experience in the collection of receivables and analysis of the outstanding balances. (See Note 4.)

#### General Property, Plant, and Equipment

General property, plant, and equipment (PP&E) represents furniture, fixtures, equipment, and information technology hardware and software, which are capitalized and depreciated or amortized over their useful lives.

CFTC capitalizes these assets if they have useful lives of at least two years and an individual value of \$25,000 or more. Bulk or aggregate purchases are capitalized when the individual useful lives are at least two years and a value of \$25,000 or more. General PP&E that do not meet these criteria are expensed when acquired. Depreciation and amortization is computed on a straight-line basis using a 5-year life. PP&E is valued net of accumulated depreciation (See Note 5.)

#### Liabilities

CFTC liabilities consist of actual and estimated amounts that are likely to be paid as a result of transactions, they are covered by budgetary resources for which Congress has appropriated funds or funding, or are otherwise available from reimbursable transactions to pay amounts due.

Liabilities include those covered by budgetary resources in existing legislation and those not yet covered by budgetary resources. All agency liabilities are funded except for the contingent liability, which will be paid if judgment is rendered against the CFTC, and the liability to pay annual leave and Federal Employee Compensation Act (FECA or workmen's compensation benefits), which will be funded by future appropriations as the leave is taken and compensation

claims are paid. All liabilities are considered current except for the annual leave liability and the Actuarial FECA liabilities.

#### Accounts Payable

Accounts payable consists primarily of contracts for goods or services, such as leases, utilities, telecommunications, and consulting and support services.

#### Accrued Payroll and Benefits

The accrued payroll and benefits represent amounts for salaries and benefits owed for the time since the payroll was last paid through the end of the fiscal year. The annual leave liability is the amount owed employees for unused annual leave as of the end of the fiscal year. Annual leave is accrued at the CFTC and represents the amount earned by employees, but not yet taken. At the end of each fiscal year, the balance in the accrued annual leave account is adjusted to reflect current balances and pay rates. Sick leave and other types of non-vested leave are expensed as taken.

The agency's employees participate in the Civil Service Retirement System (CSRS) or the Federal Employee's Retirement System (FERS). On January 1, 1987, FERS went into effect pursuant to Public Law 99-335. Most employees hired after December 31, 1983, are automatically covered by FERS and Social Security. Employees hired prior to January 1, 1984, could elect to either join FERS and Social Security or remain in CSRS.

For employees under FERS, the CFTC contributes an amount equal to one percent of the employee's basic pay to the tax deferred thrift savings plan and matches employee contributions up to an additional four percent of pay. FERS employees can contribute thirteen percent of their gross earnings to the plan. CSRS employees are limited to a contribution of eight percent of their gross earnings and receive no matching agency contribution.

The FECA provides income and medical cost protection to covered federal civilian employees injured on the job, to employees who have incurred work-related occupational diseases and to beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. The FECA program is administered by the U.S. Department of Labor (DOL), which pays valid claims against the Department and subsequently seeks reimbursement from the Department for these paid claims. Accrued FECA liability represents amounts due to DOL for claims paid on behalf of the agency.

Actuarial FECA liability represents the liability for future workers' compensation (FWC) benefits, which includes the expected liability for death, disability, medical, and miscellaneous costs for approved cases. The liability is determined using a formula provided by DOL annually, as of September 30, using a method that utilizes historical benefits payment patterns related to a specific incurred period to predict the ultimate payments related to that period. The projected annual benefit payments are discounted to present value using OMB's economic assumptions for ten-year Treasury notes and bonds. To provide more specifically for effects of inflation on liability for FWC benefits, wage inflation factors (Cost of Living Allowance) and medical inflation factors (Consumer Price Index – Medical) are applied to the calculation of projected future benefits. These factors are also used to adjust historical payment so benefits are stated in current-year constant dollars.

### Net Position

Net position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations are appropriations that have not yet been used to acquire goods and services or provide benefits. Appropriations are considered expended, or used, when goods and services have been acquired by CFTC or benefits have been provided using the appropriation authority, regardless of whether monies have been paid or payables for the goods, services, or benefits have been established. Appropriations were used primarily to acquire goods and services to operate the CFTC's programs or to provide benefits. Cumulative results of operations is the difference between the cumulative amount of expenses, exchange revenue, and transfers of assets or liabilities in or out without reimbursement.

### Revenues

The CFTC receives reimbursements and earned revenue for the following activities:

- ❖ Reimbursement for travel, subsistence, and related expenses from federal and non-federal sources for attendance at meetings or similar functions that an employee has been authorized to attend in an official capacity on behalf of the Commission.
- ❖ Reimbursement for Intergovernmental Personnel Act Mobility Program assignments from state and local governments, institutions of higher education, and other eligible organizations for basic pay, supplemental pay, fringe benefits, and travel and relocation expenses.
- ❖ Reimbursement from non-federal sources for registration fees to cover the cost of expenses related to the CFTC's annual International Regulators Conference.

### Net Cost of Operations

Net cost of operations is the difference between CFTC's expenses and its earned revenue. CFTC operates one major program with three goals, as described in the Management's Discussion and Analysis. Its mission is to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of commodity and financial futures and options, and to foster open, competitive, and financially sound futures and option markets. CFTC presents its Statement of Net Cost by goal to align the presentation of net costs with the agency's strategic plan.

### Gross Costs and Earned Revenue by Budget Functional Classification (BFC)

The CFTC's gross costs, earned revenues, and intragovernmental transactions were all related to protecting market users and the public. The BFC for CFTC is 376.

### Reconciliation of Net Obligations and Net Cost of Operations

The Statement of Financing reconciles the net obligations with the net cost of operations. Net obligations are gross obligations, adjusted by downward adjustments of prior-period obligations, less offsetting collections, as reported on the

Statement of Budgetary Resources. The net cost of operations is the difference between costs and earned revenue, as reported on the Statement of Net Cost.

The flow of the reconciliation adds to net obligations any net non-budgetary resources which are used to fund activity, but which do not appear in net obligations, such as transfers of property in or out without reimbursement, as reported on the Statement of Changes in Net Position. The combination of net obligations, or “net budgetary resources used to fund activities” and these non-budgetary resources, constitutes the total resources used to fund activities.

The reconciliation is then accomplished in part by removing any items that do not result in costs or earned revenue from the total resources used to fund activities, such as undelivered orders.

The reconciliation is finalized by adding in items in the net cost of operations that do not generate or use resources in the current period. This includes costs and earned revenues, which will never generate or use resources, such as depreciation expense. This also includes those which will generate or use resources in a future period, such as benefits expense resulting from the increase in annual leave liability, which is accrued for purposes of the Statement of Net Cost, but is not funded until the leave is taken.

#### Custodial Activity

CFTC collects penalties and fines levied against firms for violation of laws as described in the CEA as codified at 7 U.S.C. § 1, et seq, and the Commodities Futures Modernization Act of 2000, Appendix E of P.L.106-554, 114 Stat. 2763). Collections during the year are deposited to a designated fund at Treasury. Unpaid fines and penalties, with interest accrued on them, are reported as custodial receivables, with a related liability to collect them. The receivables and the liability are reduced by estimated losses from uncollectibility. Treasury reports the revenues earned and the losses from bad debts. CFTC does not retain any of the collections for reimbursement of its costs of collection.

#### Use of Management Estimates

The preparation of the accompanying financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make certain estimates and assumptions that directly affect the results of reported assets, liabilities, revenues, and expenses. Actual results could differ from these estimates.

### Note 3. Fund Balance with Treasury

Fund Balance with Treasury is related to appropriations and reimbursements for goods or services. Work performed under reimbursable agreements is initially financed by the appropriation providing the services and is subsequently reimbursed.

The status of the Fund Balance with Treasury as of September 30, 2004, is as follows:

#### **Fund Balance:**

Appropriated Funds	\$ 26,304,227
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**Status of Fund Balance with Treasury:**

Unobligated Balance Available	\$ 16,360
Unobligated Balance Expired	22,253
Unobligated Balance Unavailable	1,356,890
Obligated Balance Not Yet Disbursed	24,908,724
<b>TOTAL</b>	<b>\$ 26,304,227</b>

There are no differences between the Fund Balance with Treasury on CFTC's books and those of Treasury.

**Note 4. Accounts Receivable**

Accounts receivable consist of amounts owed to the CFTC by other Federal agencies and the public. Accounts receivable are valued net of estimated uncollectibles. Non-custodial accounts receivable are primarily for overpayments of expenses to other agencies, vendors, and employees. Historical experience has indicated that most of these receivables are collectable and there are no material uncollectible amounts.

Custodial receivables are those for which fines and penalties have been levied against businesses for violation of law. CFTC litigates against defendants for alleged violations of the Commodities Exchange Act, as amended. Violators may be subject to a variety of sanctions including fines, injunctive orders, bars or suspensions, rescissions of illegal contracts, disgorgements and restitutions to customers. Historical experience has indicated that a high percentage of these receivables prove uncollectible.

Accounts receivable as of September 30, 2004, consisted of the following:

**Category:**

<b>Intragovernmental</b>	<b>\$ 22,806</b>
<b>With the Public</b>	
<b>Custodial:</b>	
Civil Monetary Penalties, Fines, and Administrative Fees	\$ 465,735,791
Less: Allowance for Loss on Penalties, Fines and Fees	(430,332,852)
Civil Monetary Penalty Interest	65,253,060
Less: Allowance for Loss on Interest	(65,253,060)
<b>Total Custodial</b>	<b>35,402,939</b>
<b>Other</b>	<b>9,457</b>
<b>Total With the Public</b>	<b>\$ 35,412,396</b>



## Note 5. General Property, Plant, and Equipment

General Property, Plant, and Equipment as of September 30, 2004, consisted of the following:

Major Class	Service Life & Method	Acquisition Value	Accumulated Amortization/ Depreciation	Net Book Value
<b>Equipment</b>	5 Years/Straight Line	\$ 428,040	\$ 87,830	\$ 340,210
<b>IT Software</b>	5 Years/Straight Line	284,301	134,873	149,428
<b>Total</b>		\$ 712,341	\$ 222,703	\$ 489,638

## Note 6. Retirement Plans and Other Employee Benefits

CFTC imputes costs for its share of retirement systems accruing to its past and present employees, which are in excess of the amount of contributions from CFTC and its employees, which are mandated by law. The Office of Personnel Management (OPM), which administers federal civilian retirement programs, provides the cost information to CFTC. The CFTC recognizes the full cost of providing future pension and Other Retirement Benefits (ORB) for current employees as required by Statement of Federal Financial Accounting Standard (SFFAS) No. 5, *Accounting for Liabilities of the Federal Government*.

Full costs include pension and ORB contributions paid out of CFTC appropriations and costs financed by OPM. The amount financed by OPM is recognized as an imputed financing source. Reporting amounts such as plan assets, accumulated plan benefits, or unfunded liabilities, if any, is the responsibility of OPM.

Liabilities for future pension payments and other future payments for retired employees who participate in the Federal Employees Health Benefits Program and the Federal Employees Group Life Insurance Program are reported by OPM rather than CFTC.



## Note 7. Leases

The agency has no real property. The CFTC leases office space in publicly owned buildings for all of its locations. The lease contracts for publicly owned buildings are operating leases. Future lease payments are not accrued as liabilities. They are expensed as incurred. Commitments for future lease payments (in thousands) are as follows:

<b>Fiscal Year</b>	
2005	\$ 10,595
2006	11,279
2007	11,374
2008	11,752
2009	12,040
Thereafter	61,981
<b>Total Future Minimum Lease Payments</b>	<b>\$ 119,021</b>

## Note 8. Commitments and Contingent Liabilities

On November 24, 2003, The U.S. District Court held the CFTC liable for \$182,425 for violation of the Equal Access to Justice Act. The CFTC has filed an appeal in the U.S. District Court of Appeals. Although CFTC is vigorously defending this litigation, based on the initial court ruling, this amount has been recorded as a liability. It is also possible that the amount of the loss may increase by approximately \$40,000 to accommodate attorney fees at the appellate level. The amounts did not have a material effect on the financial position or results of operations as reflected in the accompanying financial statements.

## Note 9. Detailed Information on Intragovernmental Amounts

Intragovernmental assets and liabilities as of September 30, 2004, consisted of the following:

### Assets:

Fund Balance with Treasury	\$ 26,304,227
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### Accounts Receivable:

Executive Office of the President (IMF)	22,806
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<b>Total Intragovernmental Assets</b>	<b>\$ 26,327,033</b>
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Department of Labor	\$ 194,102
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<b>Total Intragovernmental Liabilities</b>	<b>\$ 194,102</b>
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## Independent Auditors' Report



KPMG LLP  
2001 M Street, NW  
Washington, DC 20036

### Independent Auditors' Report

Chairman of the U.S. Commodity Futures Trading Commission and  
Office of the Inspector General, U.S. Commodity Futures Trading Commission:

We have audited the accompanying balance sheet of the U.S. Commodity Futures Trading Commission (CFTC) as of September 30, 2004. Further, we were engaged to audit the related accompanying statements of net cost, changes in net position, budgetary resources, financing, and custodial activity for the year then ended. In connection with our engagement, we also considered CFTC's internal control over financial reporting and tested CFTC's compliance with certain provisions of applicable laws, regulations, and contracts that could have a direct and material effect on these financial statements.

#### Summary

As stated in the Opinion section, we concluded that the accompanying balance sheet is presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America. The scope of our work was not sufficient to enable us to express an opinion on the accompanying statements of net cost, changes in net position, budgetary resources, financing, and custodial activity for the year ended September 30, 2004, because the financial statements of CFTC have not been audited prior to fiscal year 2004, and as a result, we have no assurances as to the asset, liability, and obligation balances at the beginning of the year, which enter into the determination of net position as of the beginning of fiscal year 2004, and the net cost, status of budgetary resources, the reconciliation of net cost to budgetary obligations, and custodial activity for the year ended September 30, 2004.

Our consideration of internal control over financial reporting resulted in the following conditions being identified as reportable conditions:

- Recording Accruals and Preparing Financial Statements;
- Financial Accounting Process over Journal Entries;
- Financial Management Systems Need Improvement;
- Fixed Asset System;
- Recording Interest Receivable on Civil Monetary Penalties; and
- Evaluating Undelivered Orders.

We consider the first three reportable conditions, above, to be material weaknesses.

KPMG LLP, KPMG LLP, a U.S. limited liability partnership, is a member of KPMG International, a Swiss association.



The results of our tests of compliance with certain provisions of laws, regulations, and contracts disclosed the following instances of noncompliance or other matters that are required to be reported under the *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*:

- *Federal Information Security Management Act;*
- *Debt Collection Improvement Act of 1996;* and
- *Federal Financial Management Improvement Act of 1996.*

The following sections discuss our opinion on CFTC's balance sheet, the reasons why we are unable to express an opinion on the other financial statements, our consideration of CFTC's internal control over financial reporting, our tests of CFTC's compliance with certain provisions of applicable laws, regulations, and contracts, and management's and our responsibilities.

#### **Opinion on the Balance Sheet**

We have audited the accompanying balance sheet of the U.S. Commodity Futures Trading Commission as of September 30, 2004. Further, we were engaged to audit the related accompanying statements of net cost, changes in net position, budgetary resources, financing, and custodial activity for the year then ended.

The financial statements of CFTC have not been audited prior to fiscal year 2004. Therefore, we have no assurances as to the asset, liability, and obligation balances at the beginning of the year, which enter into the determination of net position as of the beginning of fiscal year 2004, and the net cost, the status of budgetary resources, the reconciliation of net cost to budgetary obligations, and custodial activity for the year ended September 30, 2004.

In our opinion, the accompanying balance sheet presents fairly, in all material respects, the financial position of CFTC as of September 30, 2004, in conformity with accounting principles generally accepted in the United States of America. Because of the matter discussed in the second paragraph of this section, the scope of our work was not sufficient to enable us to express an opinion on the accompanying statements of net cost, changes in net position, budgetary resources, financing, and custodial activity for the year ended September 30, 2004.

The information in the Management's Discussion and Analysis section is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America, or by OMB Bulletin No. 01-09, *Form and Content of Agency Financial Statements*. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information and, accordingly, we express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the balance sheet. The Performance Section is an integral part of CFTC's *Fiscal Year 2004 Performance and Accountability Report*. However, this information is not a required part of the financial statements and is presented for purposes of additional analysis. The information in the Performance Section has not been subjected to the same auditing procedures and, accordingly, we express no opinion on it.

#### **Internal Control over Financial Reporting**

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our





attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect CFTC's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements.

Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

In our fiscal year 2004 audit of CFTC's balance sheet, we noted certain matters, described in Exhibits I and II, involving internal control over financial reporting and its operation that we consider to be reportable conditions. We believe that the reportable conditions presented in Exhibit I are material weaknesses. Exhibit II presents the other reportable conditions.

\* \* \* \* \*

We also noted other matters involving internal control over financial reporting and its operation that we have reported to the management of CFTC in a two separate letters, addressing information technology and other matters, dated May 26 and November 16, 2004, respectively.

#### Compliance and Other Matters

The results of our tests of compliance with certain provisions of laws, regulations, and contracts, as described in the Responsibilities section of this report, exclusive of those referred to in the *Federal Financial Management Improvement Act* (FFMIA), disclosed two instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02, and are described below.

- Federal Information Security Management Act (FISMA).** FISMA, passed as part of the *E-Government Act of 2002*, requires that Federal agencies: (1) provide a comprehensive framework for ensuring the effectiveness of information security controls over information resources that support Federal operations and assets; (2) provide effective government-wide management and oversight of the related information security risks; (3) provide for development and maintenance of minimum controls required to protect Federal information and information systems; (4) provide a mechanism for improved oversight of Federal agency information security programs; (5) acknowledge that commercially developed information security products offer advanced, dynamic, robust, and effective information security solutions, reflecting market solutions for the protection of critical information infrastructures important to the national defense and economic security of the nation that are designed, built, and operated by the private sector; and (6) recognize that the selection of specific technical hardware and software information security solutions should be left to individual agencies from among commercially developed products. OMB Circular A-130, *Management of Federal Information Resources*, provides further information security guidance. We noted that CFTC needs continued improvement with its entity-wide security and contingency planning programs, access controls, segregation of duties, and service continuity to fully meet these guidelines.

These matters are described in our separate IT report dated May 26, 2004, and we recommend that CFTC implement the recommendations presented in that report.

- Debt Collection Improvement Act of 1996 (DCIA).** The DCIA is intended to significantly enhance the Federal Government's ability to service and collect debts. Under the DCIA,



Treasury assumes a significant role for improving government-wide receivables management. The DCIA requires Federal agencies to refer eligible delinquent non-tax debts over 180 days to Treasury for the purpose of collection by cross-servicing or the offset program. OMB Circular A-129, *Policies for Federal Credit Programs and Non-Tax Receivables*, provides further guidance on managing Federal receivables. Federal receivables, whether from credit programs or other non-tax sources, must be serviced and collected in an efficient and effective manner to protect the value of the Federal Government's assets. Interest, penalties and administrative costs should be added to all debts unless a specific statute, regulation, loan agreement, contract, or court order prohibits such charges or sets criteria for their assessment. Agencies shall assess late payment interest on delinquent debts. Agencies must adjust the interest rate on delinquent debt to conform to the rate established by a U.S. Court when a judgment has been obtained. Our tests of compliance disclosed instances where CFTC was not in compliance with certain provisions of OMB Circular A-129. Specifically, we noted that interest receivable calculations were not accurately and systematically calculated on civil monetary penalties, which CFTC collects on behalf of the Treasury.

We recommend that CFTC take corrective action to calculate interest receivable in fiscal year 2005, using the provisions of OMB Circular A-129, as further described in Exhibit II.

The results of our test of compliance with certain provisions of other laws and regulations, exclusive of those referred to in FFMIA, disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 01-02.

**FFMIA.** The results of our tests of FFMIA disclosed instances, described below and in Exhibit I, where CFTC's financial management systems did not substantially comply with Federal financial management systems requirements or Federal accounting standards.

- FFMIA mandates that Federal financial management be advanced by ensuring that Federal financial management systems can and do provide reliable, consistent disclosure of financial data, and that they do so on a basis that is uniform across the Federal government from year to year consistently, using accounting principles generally accepted in the United States of America. Federal agencies need to comply with FFMIA by adhering to policies established by OMB, such as OMB Circular A-127, *Financial Management Systems*, and OMB Circular A-130. A summary of the instances of FFMIA non-compliance detailed in our separate IT report, dated May 26, 2004, follows:
  - FFMIA requires that Federal agencies implement information security controls and contingency planning capabilities in accordance with OMB Circular A-130. CFTC needs to improve in these areas to be in compliance with Circular A-130.
  - FFMIA requires that Federal agencies implement financial systems controls in accordance with OMB Circular A-127. We noted areas where CFTC can improve the controls and processes over financial systems to better comply with Circular A-127. For example, CFTC needs to improve its funds control and financial reporting processes to fully comply with FFMIA.
- CFTC is required to prepare its financial statements in accordance with Federal accounting standards. As discussed in Exhibit I, we identified weaknesses that affected CFTC's ability to prepare its financial statements in accordance with those standards.





We recommend that CFTC implement corrective actions in fiscal year 2005 to address the recommendations in our separate IT report, dated May 26, 2004, and the recommendations in Exhibit I to this report.

The results of our tests of FFMA disclosed no instances in which CFTC's financial management systems did not substantially comply with the United States Government Standard General Ledger at the transaction level.

**Agency Response:**

The CFTC concurs and will continue its efforts to strengthen and improve its controls as recommended in this audit report.

**Responsibilities**

**Management's Responsibilities.** The *Accountability of Tax Dollars Act of 2002* requires CFTC to prepare and submit to the Congress and OMB audited financial statements. To meet this requirement, CFTC prepares annual financial statements.

Management is responsible for the financial statements, including:

- Preparing the financial statements in conformity with accounting principles generally accepted in the United States of America;
- Establishing and maintaining internal controls over financial reporting, and preparing the Management's Discussion and Analysis (including the performance measures); and
- Complying with laws, regulations, and contracts, including FFMA.

In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies. Because of inherent limitations in internal control, misstatements, due to error or fraud may nevertheless occur and not be detected.

**Auditors' Responsibilities.** As discussed in the Opinion section of this report, the scope of our work was not sufficient to enable us to express an opinion on the accompanying statements of net cost, changes in net position, budgetary resources, financing, and custodial activity, for the year ended September 30, 2004. Our responsibility is to express an opinion on CFTC's balance sheet as of September 30, 2004 based on our audit. We conducted our audit of the balance sheet in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, and OMB Bulletin No. 01-02. Those standards and OMB Bulletin No. 01-02 require that we plan and perform the audit to obtain reasonable assurance about whether the balance sheet is free of material misstatement.

An audit includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall financial statement presentation.

We believe that our audit provides a reasonable basis for our opinion on CFTC's balance sheet as of September 30, 2004.



In planning and performing our audit of CFTC's balance sheet as of September 30, 2004, we considered CFTC's internal control over financial reporting by obtaining an understanding of CFTC's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the balance sheet. We limited our internal control testing to those controls necessary to achieve the objectives described in *Government Auditing Standards* and OMB Bulletin No. 01-02. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*. The objective of our audit was not to provide assurance on internal control over financial reporting. Consequently, we do not provide an opinion thereon.

As further required by OMB Bulletin No. 01-02, with respect to internal control related to performance measures determined by management to be key and reported in the Management's Discussion and Analysis section, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions. Our procedures were not designed to provide assurance on internal control over performance measures and, accordingly, we do not provide an opinion thereon.

As part of obtaining reasonable assurance about whether CFTC's balance sheet as of September 30, 2004 is free of material misstatement, we performed tests of CFTC's compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 01-02, including certain provisions referred to in FFMIA. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations, and contracts applicable to CFTC. Providing an opinion on compliance with laws, regulations, and contracts was not an objective of our audit and, accordingly, we do not express such an opinion.

Under OMB Bulletin No. 01-02 and FFMIA, we are required to report whether CFTC's financial management systems substantially comply with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements.

#### **Distribution**

This report is intended for the information and use of CFTC's management, CFTC's Office of the Inspector General, OMB, the Government Accountability Office, and the U.S. Congress, and is not intended to be and should not be used by anyone other than these specified parties.

**KPMG LLP**

November 16, 2004



**Material Weaknesses**

Exhibit I describes the reportable conditions that are considered to be material weaknesses, and our recommendations. These matters were not identified in CFTC's FMFIA assessment. CFTC management's response is presented with each item.

**1. Improvement Needed in Recording Accruals and Preparing Financial Statements**

CFTC does not have an adequate process in place to properly estimate or record accrued liabilities during the year-end financial reporting process. At September 30, 2004, CFTC performed cut-off procedures over accounts payable in an effort to estimate the balance. During our testwork, we noted unrecorded liabilities related to fiscal year 2004 expenses for goods and services. We recommended and CFTC recorded audit adjustments for accounts payable of approximately \$855,000; operating lease liabilities of approximately \$170,000; and unfunded liabilities related to the *Federal Employees Compensation Act* (FECA) of approximately \$194,000. In addition, CFTC did not record an actuarial-related FECA accrual for future amounts due on claims incurred prior to September 30, 2004. As a result of our audit, CFTC recorded an adjustment of approximately \$514,000 for the actuarial-related FECA liability.

The need for these and other adjustments in financial statement presentation delayed CFTC in preparing its financial statements timely, and caused the agency to miss the originally established November 15, 2004 due date for submission of its *FY 2004 Performance Accountability Report* (PAR) to the Office of Management and Budget. We acknowledge that CFTC received an extension via email on November 16 to submit its PAR on November 18, 2004.

*Statements of Federal Financial Accounting Standards (SFFAS) No. 5, paragraph 19*, states that a liability for federal accounting purposes is a probable future outflow or other sacrifice of resources arising from (1) past exchange transactions; (2) government-related events; (3) government-acknowledged events; or (4) nonexchange transactions that, according to current law and applicable policy, are unpaid amounts due as of the reporting date.

SFFAS No. 1, *Accounting for Selected Assets and Liabilities*, paragraph 74, states that when an entity accepts title to goods, whether goods are received or in transit, the entity should recognize a liability for the unpaid amount of the goods. If invoices for those goods are not available when financial statements are prepared, the amounts should be estimated.

**Recommendation:**

We recommend that CFTC develop and implement procedures to identify and record accrued liabilities at year-end on a timely basis. When actual invoices have not been received, a reasonable estimate should be used. Supporting documentation should be maintained to support all estimates. CFTC also needs to develop a process to ensure that all financial reporting deadlines are met in the future.

**Agency Response:**

Management concurs with this finding and completed the adjustments to the financial statements to reflect estimated accounts payable and FECA liabilities for September 30, 2004.



**Material Weaknesses****2. Improvement Needed in Financial Accounting Process over Journal Vouchers**

CFTC's process for recording journal entries requires improvement. The process that the Office of Financial Management (OFM) uses for making entries, during the year and at year-end, does not include sufficient documentation of internal controls such as segregation of duties and supervisory review and approval of journal vouchers. We noted that the journal voucher to record the Allowance for Losses for Custodial Fines and Interest Receivable was improperly recorded, resulting in an understatement of the Allowance account and an overstatement of Custodial Fines and Interest Receivable by \$9.9 million. This item was prepared and entered into the financial system by the same lead accountant, without evidence of supervisory review.

The *Federal Managers' Financial Integrity Act of 1982* (FMFIA) requires "internal accounting and administrative controls of each executive agency shall be established in accordance with standards prescribed by the Comptroller General." The U.S. Government Accountability Office's (GAO) *Standards for Internal Control in the Federal Government* defines internal control as "an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations." *Standards for Internal Control in the Federal Government* lists examples of control activities that include (1) top-level reviews of actual performance; (2) reviews by management at the functional or activity level; (3) physical control over vulnerable assets; (4) segregation of duties; (5) proper execution of transactions and events; (6) accurate and timely recording of transactions and events; (7) access restrictions to and accountability for resources and records; and (8) appropriate documentation of transactions and internal control.

***Recommendation:***

We recommend that CFTC develop and implement internal controls related to reviewing and approving journal entries. Controls should include documented authorization of all journal entries recorded prior to entering in Federal Financial Systems (FFS) and management review of journal entries subsequent to posting in FFS. In addition, documentation should be maintained to support the rationale for posting the journal voucher.

***Agency Response:***

Management concurs with this finding. The improper recording was corrected by the Lead Accountant and reviewed and approved by the Accounting Officer. All journal vouchers generated as a result of KPMG's audit were appropriately documented by the Lead Accountant and supported, reviewed and approved by the Accounting Officer.

**Material Weaknesses****3. Financial Management Systems Need Improvement**

Effective general Information Technology (IT) controls add assurance that data used to prepare and report financial information and statements is complete, reliable, and has integrity. Our fiscal year 2004 IT assessment was focused on general IT controls over the CFTC's management systems and supporting network infrastructure, using GAO's *Federal Information System Controls Audit Manual* (FISCAM) as a guide. The six FISCAM general IT control review elements, are as follows:

- Entity-wide security program;
- Secure access controls;
- Application software development and change control;
- System software;
- Segregation of duties; and
- Service continuity.

A summary of our findings follows:

CFTC management has not finalized their risk determination for the General Support System (GSS) risk assessment. A number of policies and procedures have been prepared in draft but have not been formally approved or implemented related to: the Computer Incident Response Team, segregation of duties, the Commission-Wide Continuity of Operations Plan, and the Disaster Recovery Plan. Additionally, controls in the following areas need to be strengthened: granting system access to users; access to sensitive areas of the building; sanitizing equipment prior to disposal or reuse; and monitoring network audit logs to determine whether changes have been made within the systems; and information security testing. Environmental controls in the data center also should be improved to prevent damage to the computer equipment.

These weaknesses led to our determination that CFTC was not in compliance with the *Federal Information Security Management Act* and the *Federal Financial Management Improvement Act of 1996*, as discussed in the Compliance and Other Matters section of our auditors' report.

***Recommendations:***

Specific recommendations are included in a separate limited distribution IT general controls report dated May 26, 2004, issued as part of the fiscal year 2004 financial statement audit. We recommend that CFTC take steps to ensure effective implementation of our recommendations.

***Agency Response:***

The CFTC concurs and will continue its current efforts to strengthen and improve IT security controls.

## Exhibit II

## Reportable Conditions

Exhibit II describes other reportable conditions and our recommendations. CFTC management's response is presented with each item.

#### 4. Improvement Needed in Fixed Asset System

CFTC does not have adequate internal controls to account for, record, track, or monitor its Property, Plant, and Equipment (PP&E).

Based on discussions with OFM, and review of CFTC's fixed asset policy and records, CFTC's assets are composed of furniture, equipment, computer hardware and software, copiers, and faxes. CFTC has designated several individuals to track its fixed assets; however, the information maintained by these individuals is not complete or precise as required by Federal Accounting Standards Advisory Board (FASAB) and Joint Financial Management Improvement Program (JFMIP) standards.

In addition, CFTC has not conducted a detailed physical inventory of all property, plant, and equipment within the last three years. Partial inventories performed during the last three years by different CFTC groups have not been uniform or consistent with an established set of physical inventory policies and procedures. For example, the CFTC's Office of Information Management may perform a physical inventory using one set of guidelines and the CFTC's Office of Management Operations may use entirely different guidelines.

We used a substantive approach in auditing the balance of CFTC's PP&E and the related accumulated depreciation as of September 30, 2004. OFM manually compiled all obligations, purchase orders, and contracts related to fixed asset purchases that were recorded in FFS from 1999 through 2004, to determine total PP&E capitalizable assets. An accumulated depreciation and write-off schedule was also prepared. We determined that adjusted PP&E balances as of September 30, 2004 were fairly stated.

SFFAS No. 6, *Accounting for Plant, Property, and Equipment*, paragraph 26 states that all general PP&E shall be recorded at cost. Cost shall include all costs incurred to bring the PP&E to a form and location suitable for its intended use.

The *Federal Managers' Financial Integrity Act of 1982* requires "internal accounting and administrative controls of each executive agency shall be established in accordance with standards prescribed by the Comptroller General." GAO's *Standards for Internal Control in the Federal Government* defines internal control as "an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations." *Standards for Internal Control in the Federal Government* lists "Five Standards for Internal Control," to include monitoring. The standards further state "internal control should generally be designed to assure that ongoing monitoring occurs in the course of normal operations. It is performed continually and is ingrained in the agency's operations. It includes regular management and supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties."



## Reportable Conditions

**Recommendations:**

We recommend that CFTC:

- Develop a Property Management System that will do the following: (1) classify PP&E by assets or classes described in SFFAS 6; (2) allow user defined transaction types and automatically record the transaction type when the property record is created or updated; (3) provide unique identification; (4) provide a complete audit trail of all changes to property records including, but not limited to modifications, improvements, changes in value, and the individual entering or approving the information; (5) designate property tracked in the property management system as either capitalized or expensed; (6) allow user defined capitalization thresholds to be established for property classes; and (7) notify the user when depreciation, amortization, or depletion thresholds are exceeded.
- Establish internal controls, policies and procedures related to fixed assets to ensure that assets are recorded in the financial statements on a timely basis. CFTC should also ensure that appropriate personnel are designated to maintain adequate and timely records of inventories and property additions/disposals and that this information is communicated to the OFM on a timely basis for recording in the financial records.
- Develop procedures for property accountability that includes tracking the movement of assets, recording changes in physical condition and verification of physical counts. In addition, a unique item identification system should be implemented to track each individual asset and assist in performing physical inventories.

**Agency Response:**

Management concurs and reported these same findings in CFTC's fiscal year 2003 and 2004 FMFIA reports. We have provided copies of the reports to the auditors, which include our plans for compliance.

**5. Improvement Needed in Recording Interest on Civil Monetary Penalties**

The CFTC needs to improve its accounting for interest on Civil Monetary Penalties. We noted that interest receivable amounts assessed on delinquent custodial fines were improperly calculated. In addition, supporting documentation did not accurately substantiate the interest and penalties assessed and included on the Report on Receivables (ROR).

The *Standards for Internal Control in the Federal Government*, requires that internal control and all transactions and other significant events need to be clearly documented, and the documentation should be readily available for examination. The documentation should appear in management directives, administrative policies, or operating manuals and may be in paper or electronic form. All documentation and records should be properly managed and maintained.

In addition, OMB Circular A-129, *Policies for Federal Credit Programs and Non-tax Receivables*, Section V, Part 4: Interest, Penalties and Administrative Costs notes that Interest, penalties, and administrative costs should be added to all debts unless a specific statute, regulation, loan agreement, contract, or court order prohibits such charges or sets criteria for their assessment. Agencies shall assess late payment interest on delinquent debt. Further, agencies shall assess a penalty charge of not more than six percent (6%) per year for failure to pay a debt more than ninety (90) days past due, unless a statute, regulation required by statute, loan agreement, or contract prohibits charging interest

Exhibit II

**Reportable Conditions**

or assessing charges or explicitly fixes the interest rate or charges. A debt is delinquent when the scheduled payment is not paid in full by the payment due date contained in the initial demand letter or by the date specified in the applicable agreement or instrument. Agencies shall assess administrative costs to cover the cost of processing and handling the delinquent debt. Agencies must adjust the interest rate on delinquent debt to conform to the rate established by a U.S. Court when a judgment has been obtained.

***Recommendations:***

We recommend that CFTC's Division of Enforcement implement procedures that (1) establish controls over recording and documenting the custodial fines included in the Court Order for which the Commission will be responsible for collecting the debt; (2) establish a system which properly and accurately calculates interest and penalties on delinquent custodial fines, making sure to take into account amounts collected on the delinquent debt; (3) maintain proper records of interest calculations, collections, and support for amounts included on the ROR to Treasury, which can be readily recalculated and verified; and (4) establish a management review control which documents the reconciliation of amounts included on the ROR to supporting documentation and interest calculations.

***Agency Response:***

Management concurs with this finding and will take appropriate steps in FY 2005 to ensure compliance.

**6. Improvement Needed in Evaluating Undelivered Orders**

At the end of each quarter, OFM sends correspondence to program office official responsible for recording obligations to request the status of undelivered orders. The program office is required to review the obligation and determine if it should be deobligated. We performed test work over balances for a sample of 70 undelivered orders. We recalculated the outstanding balance without exception. We also obtained a listing of all obligations that had been outstanding for more than two years and were for goods or services that would generally not take two years for the vendor to provide. Through review of supporting documentation, we noted four items totaling approximately \$296,000 should have been deobligated, and an audit adjustment for this amount was recorded as of September 30, 2004.

CFTC's internal controls policies and procedures must ensure the status of its budgetary resources is properly recorded in the general ledger (e.g., FFS) and reported to OMB on a quarterly and year-end basis. In addition, these policies must ensure that the status of budgetary resources is properly reported in the statement of budgetary resources and the related notes to the financial statements. Budget execution procedures must be improved for CFTC to ensure that accurate, complete, and timely budgetary accounting entries are made, and that the year-end status of budgetary resources are accurately reported.

***Recommendations:***

We recommend that CFTC improve its process for analyzing the undelivered orders balance on a quarterly and year-end basis, to determine those obligations that should be deobligated. The process should ensure that OFM can accurately and timely identify those outstanding undelivered orders that should be deobligated. In addition, the Contracting Office Technical Representatives should provide

**Exhibit II**

**Reportable Conditions**

necessary documentation in a timely manner to support why outstanding obligations should remain open.

***Agency Response:***

Management concurs with this finding and will take appropriate steps in FY 2005 to ensure that accurate and timely information is provided to OFM and appropriately reflected in its financial statements.



# Appendices

- A Enforcement Litigation by Strategic Goal One
- B Enforcement Litigation by Strategic Goal Two
- C Enforcement Litigation by Strategic Goal Three
- D Acronyms





## Litigation by Strategic Goal One

### Appendix



Strategic Goal One: Ensure the economic vitality of the commodity futures and option markets.

*Energy Markets.* During FY 2004, the Commission filed a total of 12 enforcement actions resulting in \$121 million in civil monetary penalties in this program area:

- ❖ *In re CMS Marketing Services & Trading, et al.*, CFTC Docket No. 04-05 (CFTC filed Nov. 25, 2003) (settled; \$16 million civil monetary penalty)
- ❖ *In re Reliant Energy Services, Inc.*, CFTC Docket No. 04-06 (CFTC filed Nov. 25, 2003) (settled; \$18 million civil monetary penalty)
- ❖ *In re Aquila Merchant Services, Inc.*, CFTC Docket No. 04-08 (CFTC filed Jan. 28, 2004) (settled; \$26.5 million civil monetary penalty)
- ❖ *In re Oneok Energy Marketing and Trading Co., L.P., et al.*, CFTC Docket No. 04-09 (CFTC filed Jan. 28, 2004) (settled; \$3 million civil monetary penalty)
- ❖ *In re Entergy-Koch Trading, LP*, CFTC Docket No. 04-10 (CFTC Jan. 28, 2004) (settled; \$3 million civil monetary penalty)
- ❖ *In re Calpine Energy Services, L.P.*, CFTC Docket No. 04-11 (CFTC filed Jan. 28, 2004) (settled; \$1.5 million civil monetary penalty)
- ❖ *In re e prime, Inc.*, CFTC Docket No. 04-12 (CFTC filed Jan. 8, 2004) (a wholly-owned subsidiary of Xcel Energy, Inc.; settled; \$16 million civil monetary penalty)
- ❖ *In re Knauth*, CFTC Docket No. 04-15 (CFTC filed May 10, 2004) (settled; \$25,000 civil monetary penalty)
- ❖ *In re Western Gas Resources, Inc.*, CFTC Docket No. 04-17 (CFTC filed July 1, 2004) (settled; \$7 million civil monetary penalty)
- ❖ *CFTC v. NRG Energy, Inc.*, No. 04-3090 (D.Minn. filed July 1, 2004)

- ❖ *In re Coral Energy Resources, Inc.*, CFTC Docket No. 04-21 (CFTC filed July 28, 2004) (settled; \$30 million civil monetary penalty)
  
- ❖ *In re Byron G. Biggs*, CFTC Docket No. 04-22 (August 11, 2004)

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## Litigation by Strategic Goal Two

### Appendix

# B

Strategic Goal Two: Protect market users and the public.

Forex Cases. The Commission's work in fighting fraud in FY 2004 continued in the forex trading arena. The cases filed thus far during FY 2004 with respect to the offer and sale of illegal forex futures and option contracts to the general public include the following:

- ❖ *CFTC v. A.S. Templeton Group, Inc.*, NO. 03 4999 (E.D.N.Y. filed Oct. 1, 2003)
- ❖ *CFTC v. FX First, Inc., et al.*, No. SACV 03-1454-JVS(MLGx) (C.D.Cal. Filed Oct. 6, 2003);
- ❖ *CFTC v. Bibas Levy Corp., et al.*, No. 03-22624 (S.D.Fla. Oct. 7, 2003)
- ❖ *CFTC v. Rowell*, CFTC Docket No. 04-02 (CFTC filed Oct. 15, 2003)
- ❖ *CFTC v. First Lexington Group, LLC, et al.*, No. 03 CV 9124 (S.D.N.Y. Nov. 18, 2003)
- ❖ *CFTC v. Bursztyn, et al.*, No. 03 CV 9125 (S.D.N.Y. Nov. 18, 2003)
- ❖ *CFTC v. Walter, Scott, Lev & Associates, LLC, et al.*, No. 03 CV 9126 (S.D.N.Y. filed Nov. 18, 2003)
- ❖ *CFTC v. ISB Clearing Corp., et al.*, No. 03 CV 9127 (S.D.N.Y. filed Nov. 18, 2003)
- ❖ *CFTC v. Madison Deane & Associates, Inc., et al.*, No. 03 CV 9128 (S.D.N.Y. filed Nov. 18, 2003)
- ❖ *CFTC v. Itradecurrency USA LLC, et al.*, No. 03 CV 9129 (S.D.N.Y. filed Nov. 18, 2003)
- ❖ *CFTC v. Emerald Worldwide Holding, Inc., et al.*, No. CV03-8339 AHM(Ex) (C.D.Cal. filed Nov. 17, 2004)

- ❖ *In re Yost, et al.*, CFTC Docket No. 04-07 (CFTC filed Dec. 22, 2003)
- ❖ *CFTC v. Erskine, et al.*, No. 1:04oV0016 (N.D.Ohio filed Jan. 6, 2004)
- ❖ *CFTC v. Clearview Capital Mgt., et al.*, NO. 04cv45(FSH) (D.N.J. filed Jan. 8, 2004)
- ❖ *CFTC v. Gibraltar Monetary Corp., et al.*, No. 04-80132 (S.D.Fla. Filed Feb. 10, 2004)
- ❖ *CFTC v. FxTrade Financial, LLC, et al.*, No. 04-2181-Dan (W.D.Tenn. Filed March 17, 2003)
- ❖ *CFTC v. E Net Speculation Ltd., et al.*, No. 3:04CV169-s (W.D.Ky. Filed March 19, 2004);
- ❖ *CFTC v. Calvary Currencies LLC, et al.*, NO. 8:04-CV-01021-DKC (D.Md. Filed March 29, 2004)
- ❖ *CFTC v. Lexington Royce & Associates*, No. 04 CV 02768 (S.D.N.Y. filed April 12, 2004)
- ❖ *CFTC v. Axxess Trade Co., Inc.*, No. 04 CV 4293 (S.D.N.Y. filed June 7, 2004)
- ❖ *CFTC v. Sterling Financial Group, Inc.*, No. 04-21346 CIV-LENARD (S.D.Fla. filed June 7, 2004)
- ❖ *CFTC v. Next Financial Services Unlimited, Inc., et al.*, No. 04-80562 CIV-RYSKAMP (S.D.Fla. June 21, 2004)
- ❖ *CFTC v. Global Atlantic Management, Inc., et al.*, No. 04-60797 CIV-JORDAN (S.D.Fla. filed June 21, 2004)

During FY 2004, the Commission also achieved the following significant litigation results in actions filed in this practice area during previous fiscal years:

- ❖ *CFTC v. Hawker, et al.*, No. 2:03 CV 0260 JTG Consent Order Of Permanent Injunction And Other Equitable Relief [Against Bryan Keith Hawker and G, Hawker & Stone, LLC] (D.Utah entered Oct. 24, 2003) (forex fraud case filed March 12, 2003; permanent injunction; restitution and civil monetary penalty reserved for further proceedings)
- ❖ *CFTC v. Offshore Financial Consultants, Inc, et al.*, NO. 02-60769-CIV-MORENO, Default Final Judgment (S.D.Fla. entered Nov. 10, 2003)

- (forex fraud case filed April 30, 2001; permanent injunction against Anthony Garcia and James Sexton; civil monetary penalties against Garcia (\$360,000) and Sexton (\$360,000))
- ❖ *CFTC v. A.S. Templeton Group, Inc.*, NO. 03 4999, Order Of Permanent Injunction (E.D.N.Y. entered Nov. 24, 2003) (forex fraud case filed Oct. 1, 2003; permanent injunction (Michael Vitebsky and Boris Shuster))
  - ❖ *CFTC v. World Banks Foreign Currency Traders, Inc. et al.*, No. 01-7402, Consent Order Of Permanent Injunction And Other Equitable Relief Against Defendants Frank Desantis, Christopher Boutche And Erin Valko (S.D. Fla. entered Jan. 20, 2004)(forex fraud case filed August 23, 2001; permanent injunction; \$600,000 total restitution (DeSantis & Boutchie \$300,000 each))
  - ❖ *CFTC v. Elsesser, et al.*, No. 8:03-CV-681-T-23TBM Consent Order Of Permanent Injunction And Other Equitable Relief Against Defendant Keith Elsesser (M.D.Fla. entered Jan. 26, 2004) (forex fraud case filed April 11, 2003; permanent injunction; \$73,507 restitution; \$120,000 civil monetary penalty)
  - ❖ *CFTC v. Fintrex, Inc., et al.*, No. CV 01-06907 PA (CWx), Final Order Of Default Judgment Against Fintrex, Inc., And Arman Ovsepyan (C.D.Cal. entered Jan. 29, 2004) (forex fraud case filed August 9, 2001; permanent injunction; \$1,320,283 (Fintrex), and \$683,670 (Fintrex and Ovsepyan, jointly and severall) restitution; \$4,007,906 (Fintrex) and \$1,367,340 (Ovsepyan) civil monetary penalties; and pursuant to the court's December 12, 2002 civil contempt order, Ovsepyan is further ordered to return funds to Fintrex of \$170,012 and make an accounting of disposition of other assets)
  - ❖ *CFTC v. Bibas Levy Corp., et al.*, No. 03-22624, Final Default Judgment (S.D.Fla. entered April 16, 2004) (forex fraud case filed October 7, 2003; \$351,686 restitution; \$100,013 disgorgement; \$120,000 civil monetary penalty; monetary penalties to be paid jointly and severally by Bibas Levy Corp., Zacarias Bibas, and Hassan Sharam)
  - ❖ *CFTC v. Noble Wealth Data Information Services, Inc., et al.*, No. PJM 98-3316, Settlement Order (D.Md. entered May 14, 2004) (forex fraud case filed October 1, 1998; permanent injunction against Esfand Baragosh; \$5,264,251 restitution; \$1,211,058 civil monetary penalty)
  - ❖ *CFTC v. Eurobancorp, et al.*, No. 03-767 SJO (JWJx) Orders Of Permanent Injunction And Other Equitable Relief Against Defendants Paris DeLesseppes, and John Lassen (C.D.Cal. entered May 21 and 28, 2004) (forex fraud case filed February 3, 2003; permanent injunction; \$333,769 (Lassen) and \$333,769 (DeLesseppes) restitution; \$240,000 (Lassen) and \$240,000 (DeLesseppes) civil monetary penalties)
  - ❖ *CFTC v. International Financial Services (New York), Inc., et al.*, No. 02 Civ. 5497 (GEL), Final Judgment [Against All Defendants] (S.D.N.Y. entered May 26, 2004) (forex fraud case filed July 17, 2002; permanent injunction; \$25,428,840 (jointly and severally) restitution and disgorgement; and \$76,286,520 (jointly and severally) civil monetary penalty)

- ❖ *CFTC v. O'Neill, et al.*, No. 02-61307-Civ-Gold, Order of Permanent Injunction and Supplemental Order Of Judgment On Restitution And Civil Monetary Penalties Against [Donald O'Neill and Danielle O'Neill] (S.D. Fla. entered Nov. 14, 2003 and June 15, 2004) (forex fraud case filed September 17, 2002; permanent injunction; \$11,519,660 restitution; \$10,609,133 civil monetary penalty)
- ❖ *CFTC v. Wheeler, et al.*, No. 6:03CV42, Consent Orders Of Disgorgement As To Relief Defendants Mendoza, Gary Wood, Michael Fagan, and Walter Cole (E.D.Tex. entered June 4, 15 and 16, 2004) (forex fraud case filed January 30, 2003; ordered disgorgement of \$50,000 (Mendoza), \$92,000 (Fagan), \$318,170 (Cole), and \$500,000 (Wood))

*Commodity Pools, Hedge Funds And Commodity Pool Operators.* During FY 2004, the Commission filed the following enforcement actions in this program area:

- ❖ *CFTC v. Marquis Financial Mgt. Systems, Inc., et al.*, No. 03-74206 (E.D.Mich. Filed Oct. 20, 2003)
- ❖ *CFTC v. Friedlander, et al.*, No. 03 CV 8319 (S.D.N.Y. filed Oct. 21, 2003)
- ❖ *CFTC v. Boston Trading Advisors, LLC, et al.*, CFTC Docket No. 04-03 (CFTC filed Oct. 27, 2003)
- ❖ *CFTC, et al. v. Silberstein*, No. 1:04-CV-666 (D.Md. Filed March 5, 2004); *CFTC v. Equity Financial Group LLC, et al.*, No. 04CV1512 (D.N.J. filed April 1, 2004)
- ❖ *CFTC v. Weatherford*, No. CV04-4079 SJO(CWz) (C.D.Cal. filed June 8, 2004)
- ❖ *CFTC v. Vanguard Financial Mgt. Assoc., et al.*, No. SAVC 04-575(GLT) (C.D.Cal. filed May 19, 2004)

During FY 2004, the Commission also achieved the following significant litigation results in actions filed in this practice area during previous fiscal years:

- ❖ *CFTC v. Brockbank, et al.*, No. 2:00 CV 00622ST, Consent Order Of Permanent Injunction And Other Ancillary Relief Against Defendant Thomas E. Jones (D.Utah entered Oct. 30, 2003) (commodity pool fraud case filed August 8, 2003, amended January 16, 2003; permanent injunction; \$74,000 restitution)
- ❖ *CFTC v. Mady et al.*, No. 02-72364, Consent Order Of Permanent Injunction And Other Equitable Relief And A Civil Monetary Penalty Against Defendant Charles G. Mady (E.D. Mich. entered Nov. 6, 2003) (pool fraud case filed June 11, 2002; permanent injunction; undertaking to not seek registration and to not trade for 10 years; \$8,220,860 restitu-

tion; \$8,220,860 civil monetary penalty with dollar for dollar credit for payment towards restitution)

- ❖ *CFTC v. Chilcott, et al.*, No. 2:02-cv-94-FtM-29SPC, Order [Against Ted E. Whidden] and Supplemental Consent Order Concerning Restitution And Civil Monetary Penalty Against Defendants Thomas D. Chilcott And Leona Westbrook (M.D.Fla. entered Dec. 16, 2003, and January 6, 2004) (commodity pool fraud case filed March 6, 2002; \$2,279,521 restitution (joint and several by Whidden, Chilcott and Westbrook); civil monetary penalties of \$1,320,000 (Chilcott) and \$110,000 (Westbrook))
- ❖ *CFTC v. Sovereign Resource Management, Inc., et al.*, No. 02-1783 Order Of Default Judgment For Permanent Injunction And Other Ancillary Relief Against Defendants Sovereign Resource Management, Inc., Ken Mitra and Virgil E. Smith (D. Minn. entered March 26, 2004) (commodity pool fraud case filed July 18, 2002; permanent injunction; \$3,127,752 restitution (joint and several); civil monetary penalties of \$550,000 (Sovereign), \$660,000 (Mitra) and \$440,000 (Smith))

Commodity Trading Advisors, Managed Accounts, And Trading Systems. The Commission filed the following enforcement actions in this program area during FY 2004:

- ❖ *CFTC v. Matrix*, CFTC Docket No. 04-01 (CFTC filed Oct. 2, 2003)
- ❖ *In re Harrison*, CFTC Docket No. 04-04 (CFTC filed Nov. 18, 2003)
- ❖ *CFTC v. Profit Partners, Inc.*, No. CV03-9190 (C.D.Cal. filed Dec. 16, 2003)
- ❖ *In re Allen*, CFTC Docket No. 04-14 (CFTC filed April 9, 2004)

During FY 2004, the Commission also achieved the following significant litigation results in actions filed in this practice area during previous fiscal years:

- ❖ *CFTC v. Lee, et al.*, No. 4:02CV 01477 CAS, Consent Order Of Permanent Injunction And Other Equitable Relief And A Civil Monetary Penalty Against Defendants Kenneth J. Lee And KJL Financial Group, Inc. (E.D. Mo. ordered March 9, 2004) (managed accounts case filed September 30, 2002; permanent injunction; restitution \$567,551 (joint and several); \$300,000 civil monetary penalty (Lee)); and
- ❖ *CFTC v. Goldman*, No. 03-3265 JFW (RCx), Consent Order Of Permanent Injunction And Other Equitable Relief Against Defendant Oscar Goldman (C.D.Cal. entered April 1, 2004) (CTA fraud case filed May 9, 2003; permanent injunction; \$95,500 disgorgement; \$180,000 civil monetary penalty).

Introducing Brokers And Their Associated Persons. During FY 2004, as in past years, the Commission devoted time and attention to matters involving violations by IBs and their APs. Such cases often involve fraudulent misrepresentations,



usually to retail customers, to induce them to invest. The Commission has filed the following enforcement actions in this practice area during FY 2004:

- ❖ *CFTC v. Commercial Hedge Services, et al.*, No. 4:04CV3184 (D.Neb. filed May 5, 2004)
- ❖ *CFTC v. First American Investment Services, Inc.*, No. 04-60744 CIV-HURLEY (S.D.Fla. filed June 7, 2004)

Futures Commission Merchants. During FY 2004, the Commission filed the following case in this enforcement program area:

- ❖ *CFTC v. Krysinski*, No. 03C 8571(N.D.Ill. Filed Nov. 26, 2003)

Statutory Disqualifications. During FY 2004, the Commission filed the following enforcement actions in this program area:

- ❖ *In re FX First, Inc.*, CFTC Docket No. SD 04-01 (CFTC filed Feb. 18, 2004)
- ❖ *In re VanPatten*, CFTC Docket No. SD 04-02 (CFTC filed March 25, 2004)
- ❖ *In re Anixter*, CFTC Docket No. SD 04-03 (CFTC filed June 30, 2004)

Quick Strike Cases. The Commission is committed to responding quickly to enforcement investigations that uncover ongoing fraud. Quick-strike cases are civil injunctive actions that generally are filed in Federal district courts within days or weeks of the discovery of the illegal activity, enabling the Commission to stop fraud at an early stage and to attempt to preserve customer funds. Thus far during FY 2004, the Commission filed the following ten quick-strike cases:

- ❖ *CFTC v. Bibas Levy Corp., et al.*, No. 03-22624 (S.D.Fla. Oct. 7, 2003) (forex fraud)
- ❖ *CFTC v. Krysinski*, No. 03C 8571(N.D.Ill. Filed Nov. 26, 2003) (FCM fraud)
- ❖ *CFTC v. Profit Partners, Inc.*, No. CV03-9190 (C.D.Cal. filed Dec. 16, 2003) (commodity trading system fraud)
- ❖ *CFTC v. Silberstein*, No. 1:04-CV-666 (D.Md. filed March 5, 2004) (CPO fraud)
- ❖ *CFTC v. FxTrade Financial, LLC, et al.*, No. 04-2181-Dan (W.D.Tenn. filed March 17, 2003) (forex fraud)

- ❖ *CFTC v. Lexington Royce & Associates*, No. 04 CV 02768 (S.D.N.Y. filed April 12, 2004) (forex fraud)
- ❖ *CFTC v. Vanguard Financial Mgt. Assoc., et al.*, No. SAVC 04-575(GLT) (C.D.Cal. filed May 19, 2004) (CPO fraud)
- ❖ *CFTC v. Weatherford*, No. CV04-4079 SJO(CWz) (C.D.Cal. filed June 8, 2004) (CPO fraud)
- ❖ *CFTC v. Next Financial Services Unlimited, Inc., et al.*, No. 04-80562 CIV-RYSKAMP (S.D.Fla. June 21, 2004) (forex fraud)
- ❖ *In re Anixter*, CFTC Docket No. SD 04-03 (CFTC filed June 30, 2004) (statutory disqualification)

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## Litigation by Strategic Goal Three

### Appendix



Strategic Goal Three: Ensure market integrity to foster open, competitive, and financially sound markets.

Trade Practice. During FY 2004, the Commission filed the following enforcement actions in this program area:

- ❖ *CFTC v. Olam Int'l Ltd.*, CFTC Docket No. 04-13 (CFTC filed April 6, 2004)
- ❖ *In re Barry Callebaut Sourcing AG*, CFTC Docket No. 04-16 (CFTC filed May 13, 2004)

International Cooperative Enforcement. The Commission continues to coordinate enforcement activities with foreign authorities. During FY 2004 (October 1, 2003 to July 13, 2004), the Commission made 93 requests for assistance to 45 foreign authorities, and it received 23 requests from authorities in foreign jurisdictions. The number of requests made to and received from foreign authorities in FY 2004 have already exceeded the number of requests for the entire FY 2003. In particular this year, the Commission was successful in obtaining assistance, including bank records, in several jurisdictions where we did not have prior co-operative relationships.

The Enforcement Division also has devoted time and resources to matters involving allegations that persons or entities have committed fraud or other misconduct in their cross-border activities. Such misconduct can adversely affect U.S. firms as well as customers located in the U.S. and overseas. The Commission's efforts in this area during FY 2004 included the filing of the following enforcement actions:

- ❖ *CFTC v. A.S. Templeton Group, Inc.*, No. 03 4999 (E.D.N.Y. filed Oct. 1, 2003)
- ❖ *CFTC v. FX First, Inc., et al.*, No. SACV 03-1454-JVS (MLGx) (C.D. Cal. filed Oct. 6, 2003)
- ❖ *CFTC v. Marquis Financial Mgt. Systems, Inc., et al.*, No. 03-74206 (E.D. Mich. filed Oct. 20, 2003)
- ❖ *CFTC v. Walter, Scott, Lev & Associates, LLC, et al.*, No. 03 CV 9126 (S.D.N.Y. filed Nov. 18, 2003)

- ❖ *CFTC v. ISB Clearing Corp., et al.*, No. 03 CV 9127 (S.D.N.Y. filed Nov. 18, 2003)
- ❖ *CFTC v. Itradecurrency USA LLC, et al.*, No. 03 CV 9129 (S.D.N.Y. filed Nov. 18, 2003)
- ❖ *CFTC v. Emerald Worldwide Holding, Inc., et al.*, No. CV03-8339 AHM (ex) (C.D.Cal. filed Nov. 17, 2004)
- ❖ *CFTC v. Gibraltar Monetary Corp., et al.* No. 04-80132 (S.D.Fla. filed Feb. 10, 2004)
- ❖ *CFTC v. Silberstein*, No. 1:04-CV-666 (D.Md. filed March 5, 2004)
- ❖ *CFTC v. E Net Speculation ltd., et al.*, No. 3:04 CV 169-s (W.D.Ky. filed March 17, 2004)
- ❖ *CFTC v. Calvary Currencies LLC, et al.*, No. 8:04-CV-01021-DKC (D.Md. filed March 29, 2004)
- ❖ *CFTC v. Equity Financial Group LLC, et al.*, No. 04CV1512 (D.N.J. filed April 1, 2004)
- ❖ *CFTC v. Lexington Royce & Associates*, No. 04 CV 02768 (S.D.N.Y. filed April 12, 2004)
- ❖ *CFTC v. Axxess Trade Co., Inc.*, No. 04 CV 4293 (S.D.N.Y. filed June 7, 2004)
- ❖ *CFTC v. Sterling Trading Group, Inc.*, No. 04-21346 CIV-Lenard (S.D.Fla. filed June 7, 2004)

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## Table of Acronyms

Appendix

D

ALJ	Administrative Law Judge
AML	Anti-Money Laundering
AP	Associated Person
AWB	Australian Wheat Board
BSE	Bovine Spongiform Encephalopathy
CEA	Commodity Exchange Act
CFTC	Commodity Futures Trading Commission
CFMA	Commodity Futures Modernization Act of 2000
COSRA	Council of Securities Regulators of the Americas
CPO	Commodity Pool Operator
CSCE	Coffee Sugar and Cocoa Exchange
CSRS	Civil Service Retirement System
CTA	Commodity Trading Advisor
DART	Designation and Rule Tracking
DCO	Derivatives Clearing Organizations
DMO	Division of Market Oversight (CFTC)
DOI-NBC	Department of Interior's National Business Center
DOL	Department of Labor
DOJ	Department of Justice
DTEF	Derivatives Transaction Execution Facility
eTS	eTravel Service
FB	Floor Broker
FBI	Federal Bureau of Investigation
FCM	Futures Commission Merchant
FERS	Federal Employees Retirement System
FIRREA	Financial Institutions Reform, Recovery, and Enforcement Act of 1989
FMFIA	Federal Managers' Financial Integrity Act
FOIA	Freedom of Information Act
FOREX	Foreign Currency
FSA	U.K. Financial Service Authority
FTE	Full-time Equivalent
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
HTA	Hedge To Arrive
IA	Investment Advisor
IB	Introducing Broker
IFSRA	Irish Financial Services Regulatory Authority
ISS	Integrated Surveillance System
IOSCO	International Organization of Securities Commissions
IRS	Internal Revenue Service
JO	Judgment Officer
MASC	Management Accounting Code Structure
MDA	Management's Discussion and Analysis
MGE	Minneapolis Grain Exchange
MOU	Memorandum/Memoranda of Understanding

## FY 2004 PERFORMANCE AND ACCOUNTABILITY REPORT

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MMOU	Multilateral Memorandum of Understanding
NFA	National Futures Association
NFC	National Finance Center
NYMEX	New York Mercantile Exchange
OCE	Office of the Chief Economist (CFTC)
OFM	Office of Financial Management (CFTC)
OGC	Office of the General Counsel
OHR	Office of Human Resources (CFTC)
OIA	Office of International Affairs (CFTC)
OIRM	Office of Information Resources Management (CFTC)
OMB	Office of Management and Budget
OPM	Office of Personnel Management
ORB	Other Retirement Benefits
RWG	Registration Working Group
SC4	Standing Committee 4 on Enforcement and Information-Sharing
SC5	Standing Committee 5 on Investment Management
SEC	Securities and Exchange Commission
SFE	Sydney Futures Exchange
SFP	Security Futures Products
SHIMS	Safety and Health Information Management System
SOI	Statement of Intent
SPARK	Stress Positions at Risk
SRO	Self-Regulatory Organization
USA PATRIOT	Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism
UK	United Kingdom



